

Rating-Agentur Expert RA GmbH confirmed at 'B' the sovereign government rating and at 'CCC' the credit climate rating of Uzbekistan

Rating-Agentur Expert RA GmbH confirmed the sovereign government credit rating (SGC) of Uzbekistan 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.

Rating-Agentur Expert RA GmbH confirmed the country credit environment rating (CCE) of Uzbekistan at 'CCC+' (low quality of credit environment of the country) in national currency and at 'CCC' (low quality of credit environment of the country) in foreign currency.

MAJOR FACTORS THAT INFLUENCED BOTH TYPES OF RATINGS:

Positive factors:

- Gross government debt according to IMF stood at around 14,8% of GDP and 45,7% of budget revenues in 2016 and remained the lowest among Uzbekistan's regional peers;
- Historically low short-term debt remains a significant positive factor, which we estimate at 1,04% of GDP for 2016;
- FX reserves, at 45% of GDP, continue to be relatively high covering gross government debt by more than 3x and short-term government debt by more than 40x;
- Despite a drop in the fiscal surplus fueled by lower tax collection and higher expenditures, the fiscal budget is forecasted to remain balanced in 2016. However it is expected to continue its negative trend due to an increase in government spending;
- Real GDP increased by around 6% in 2016 (one of the highest real GDP growth rates among Uzbekistan's regional peers). However, the regional spillovers (causing remittances to fall sharply and exports to decline) and low commodities' prices, may pose a threat to this high growth rate's long-term sustainability;
- Even though the banking sector remains undeveloped, the risk position of the industry is positive with NPLs at 0,44% of total loans in 2016 and capital to assets ratio at 11,1% in 2016 according to data from the World Bank;
- Uzbekistan's long-term growth perspectives are supported by a significant amount of natural resources (mainly natural gas, gold and cotton) and a solid investment potential evidenced by a high volume of national savings to GDP level of 31% in 2016.

Restricting factors:

- Uzbekistan has adopted a fiscal policy focused on social spending which, despite a difficult macroeconomic situation, helped to sustain growth at very high levels (the highest amongst its regional peers). This, among other factors, has eroded the fiscal balance to almost a zero figure relative to GDP 2016. However, the level of fiscal balance and government indebtedness of Uzbekistan remains the lowest within its regional peers and does not pose a significant risk;
- Due to the recent expansionary fiscal policy, the government debt, according to IMF, is estimated to increase substantially in 2016 by 60% y-o-y. As a result, the gross government debt relative to GDP is set to increase by 4 p.p. in the same period;

- The country carries out a rather open and clear privatization plan mainly through the auctions managed by a separate government entity. However, no budget-significant funds have been raised so far and the scope of the activity remained low;
- The Central Bank has kept the reference rate at 9% since it trimmed it from 10% in January 2015. This reflects a loose monetary policy as inflation remains substantial.

Negative factors:

- The country stays one of the least developed in the region as shown by the low level of GDP per capita, estimated at USD 6 453 in 2016, and HDI index of 0,57 in 2015;
- Despite the fact, that the inflation rate has exhibited a positive dynamic in the last three years, decreasing by 0,84 p.p. (according to IMF), it remained high, estimated at around 8,4% in 2016;
- The unemployment rate, as reported by the World Bank, was high at 10,6% in 2014;
- Despite Banks' assets having grown by 23% in 2016, the size of the banking sector remains limited. This is reflected by low bank's asset and private credit volumes relative to GDP at 40% and 22% in 2016 respectively;
- Stagnant institutional development with low transparency and quality of official statistics and high level of corruption in the country (ranked 156th out of 176 countries in 2016 according to Transparency International);
- The proportion of state-owned banks (SOBs) in the banking system remains very high (about 80% of total bank assets at end-2014). Despite this, the major SOBs remain strong and stable with low NPLs and acceptable levels of liquidity;
- The capital market of Uzbekistan is rather undeveloped with only 184 listed companies on the national stock exchange as of March 2017 and market capitalization as low as 4,5% of GDP as of 3Q 2016. At the same time, the ten most active issuers effectively make the market with 98,8% of total trades.

Stress factors:

- Despite the announcement of the plans to change the FX policy in 2017, so far the government keeps the capital controls, leading to currency black markets and other distortions, unchanged. Since 2009 the difference between the official and parallel (black market) exchange rate increased significantly. This situation generates speculation in the FX market, volatility of exchange rate and low FDI. It also contributes to the risks of money laundering and unrecorded capital flows (moderate stress-factor).

Currency risks:

- Most of the total gross government debt is of an external nature. Additionally, restrictions to operate in foreign currency, the parallel FX market and the obligation for exporters to surrender a partial or full amount of their FX proceeds continue to constitute the main currency risk of Uzbekistan.

ADDITIONAL FACTORS THAT INFLUENCED CCE RATINGS:

Negative factors:

- Subdued quality and quantity of instruments in the local financial market;
- Banks' credit policy is influenced by state-directed lending, often below market rates.

Restricting factors:

- Low protection of investors as evidenced by the ranking of Doing Business (Uzbekistan ranked 70th out of 180 countries in 2016) (despite turning positive is kept in the restricting zone).

SENSITIVITY ASSESSMENT:

The following developments could lead to an upgrade:

- Successful implementation of reforms, meant to lift capital controls and liberalize FX market;
- Improvement in the external environment along with further development of the financial sector and transparency of national institutions.

The following developments could lead to a downgrade:

- Continued deterioration of the fiscal balance and accumulation of government debt.

“The ratings of Uzbekistan continue to be supported by the very low levels of short- and long-term debt, which are well covered by the accumulated FX reserves. Noticeably high GDP growth rates and balanced government budget, despite regional instability and increased social expenditure, positively affected the ratings.

On the negative ground, the short-term orientation of the current fiscal policy, as well as the inability of the CBU to curb inflation continue to constrain the ratings. Capital controls and the parallel FX market, combined with underdeveloped financial institutions and rather unfavorable business environment had a negative effect on the ratings. However, a lot will depend on how well the recently elected president, Shavkat Mirziyoyev, will implement the initiatives designed to liberalize political and economic environment of Uzbekistan.” – Clarified Ilya Makunin, Rating Analyst of Rating-Agentur Expert RA GmbH.

Responsible expert: Ilya Makunin, Rating Analyst of Rating-Agentur Expert RA GmbH

Reviewer: Gustavo Angel, Rating Associate of Rating-Agentur Expert RA GmbH

Research report on Uzbekistan is available at:

http://raexpert.eu/reports/Research_report_Uzbekistan_24.03.2017.pdf

Next scheduled rating publication: 22 September 2017. The full sovereign rating calendar can be found at <http://raexpert.eu/sovereign/#conf-tab-5>

For further information contact:

Rating-Agentur Expert RA GmbH
Walter-Kolb-Strasse 9-11,
60594 Frankfurt am Main, Germany
+49 (69) 3085-45-00
E-mail: info@raexpert.eu
www.raexpert.eu

RATING HISTORY:

Date	Review reason	SGC		CCE	
		National currency	Foreign currency	National currency	Foreign currency
23.09.2016	Scheduled revision of both types of ratings for the country	B+	B	CCC+	CCC
15.04.2016	First assignment of both types of ratings for the country	B+	B	CCC+	CCC

Minute's summary

The rating committee for Uzbekistan was held on 23 March 2017. 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 and Country Credit Environment Ratings. Short Public Version (from April 2015) can be found under the following link: <http://raexpert.eu/files/methodology/Methodology-Short-Sovereign.pdf>. Descriptions and definitions of all rating categories can be found under the following link: <http://raexpert.eu/sovereign.php> 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.

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

Main sources of information: International Monetary Fund, World Bank, CIA Fact book, World Economic Forum, Doing Business, United Nations, The State Committee of the Republic of Uzbekistan on Statistics, Central Bank of Uzbekistan (CBU), Ministry of Finance of Uzbekistan, Transparency International.

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.

Despite similar methodologies, credit ratings of Uzbekistan from RAEX (Moscow) (both SGC and CCE) may be different from those assigned by Rating-Agentur Expert RA GmbH due to:

- Possible differences in expert assessments of individual factors;
- Some differences in methodologies (methodologies are similar but not identical);
- Differences in the date/period of assessment for individual factors.

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

The Agency disclaims all liability in connection with any consequences, interpretations, conclusions, recommendations and other actions directly or indirectly related to the conclusions and opinions contained in the Agency's Research Reports.

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.