# Research Report on Tajikistan

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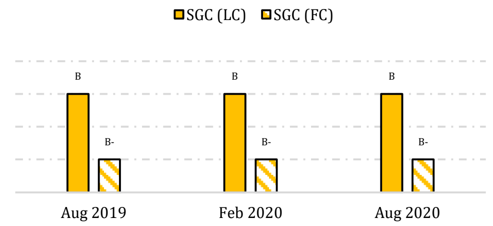
**Ratings**

| | |
|---|---|
| Sovereign Government Credit (LC) | B |
| Sovereign Government Credit (FC) | B- |
| Outlook (LC) | Negative |
| Outlook (FC) | Negative |

* These ratings are unsolicited

**Ratings dynamics**




**Main Economic Indicators of Tajikistan**

| Macro indicators | 2017 | 2018 | 2019 |
|---|---|---|---|
| Gross gov. debt, TJS bn | 31 | 33 | 34 |
| Nominal GDP, TJS bn | 61 | 69 | 77 |
| Real GDP growth, % | 7,6 | 7,3 | 7,5 |
| Gross gov. debt/GDP, % | 50,4 | 47,9 | 44,6 |
| Deficit (surplus)/GDP, % | -6,0 | -2,8 | -2,1 |
| Inflation rate, % | 6,7 | 5,4 | 8,0 |
| Current Account Balance/GDP, % | - | - | -2,3 |
| External debt, USD bn | - | - | 5,5 |

| Development indicators | 2019 |
|---|---|
| Inequality adj. HDI | 0,57* |
| GDP per capita, USD th | 3,6 |

| Default indicator | 07.08.2020 |
|---|---|
| 7Y Gov Bond Yield, % | 9,2** |

Source: RAEX-Europe calculations based on data from the IMF, WB, NBT.
* 2018 data; **Maturity in 2027.

## Summary

The Agency has confirmed Tajikistan's ratings at 'B-' in FC and 'B' in LC with a negative outlook. The confirmation of the ratings is based on the mitigation of the debt repayment risks in the short- and mid-run perspective due to significant financial support from international financial organizations on concessional terms.

In the long-term perspective, the ratings and the outlook reflect deterioration of the debt and fiscal position of the government on the back of the COVID-19 crisis, low level of welfare and high unemployment, subdued and undeveloped financial system, as well as the lingering risk of materialization of contingent liabilities.

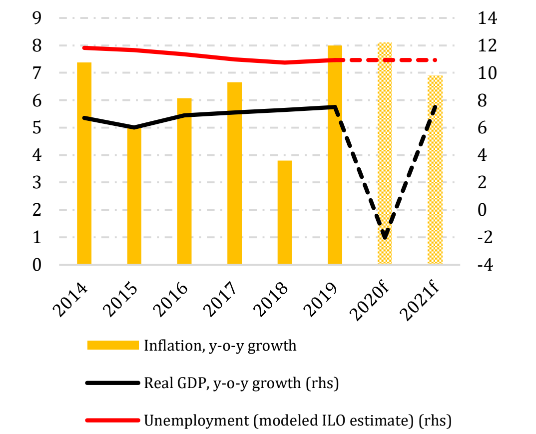
In addition, the external position of the government remains very fragile with a high share of FX-denominated debt, dependence on imports and remittances, low level of export to GDP, and elevated dollarization of the financial system.

**A contraction of up to 2% is expected in 2020, although national wealth and institutional development remain weak.** Before the COVID-19 crisis, economic developments were favorable in Tajikistan, the economy grew by more than 7% yearly over the last three years, which is one of the highest readings in the region, supported by agriculture, industry, and services. However, the global pandemic already affected economic activity substantially in 1H 2020. While the government didn't report any confirmed COVID-19 cases till end of April, the authorities have taken containment measures to prevent an outbreak. Cross-border transport restrictions with trading partners have significant negative effect on industrial production, construction, and services. In addition, the sharp decline in oil prices and travel disruptions with Russia have affected migrant worker mobility and remittances inflow, which declined by almost 50% y-o-y in March.

We expect the deepest economic slowdown will be reported in 2Q-3Q 2020, with a slow recovery by the end of the year. As a result, the overall contraction by 2% is expected in 2020 due to a sharp trade slowdown, limitations on migrant worker mobility and remittances, and disruptions in mining, services, and construction (see graph 1).

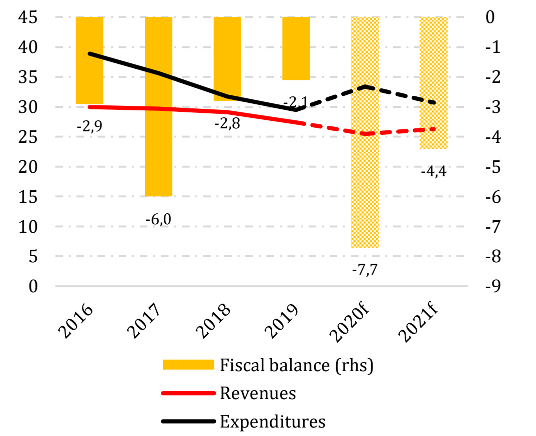
In the long-term perspective, the government creditworthiness still limited by high and volatile unemployment rates, low level of institutional

**Graph 1:** Macroeconomic indicators, %



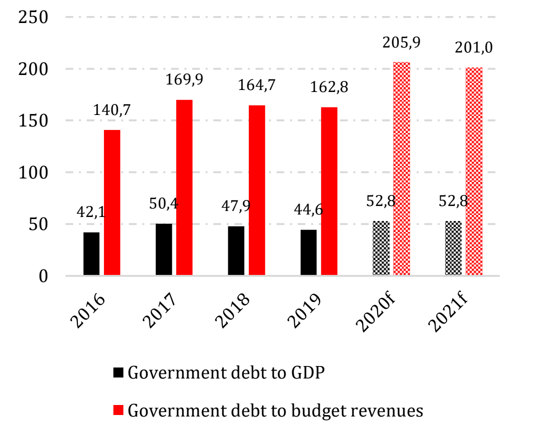

Source: RAEX-Europe calculations based on data from the WB, IMF, NBT

**Graph 2:** Fiscal budget dynamics, % of GDP




Source: RAEX-Europe calculations based on data from the WB, IMF, NBT

**Graph 3:** Government debt dynamics, %




Source: RAEX-Europe calculations based on data from the WB, IMF, NBT

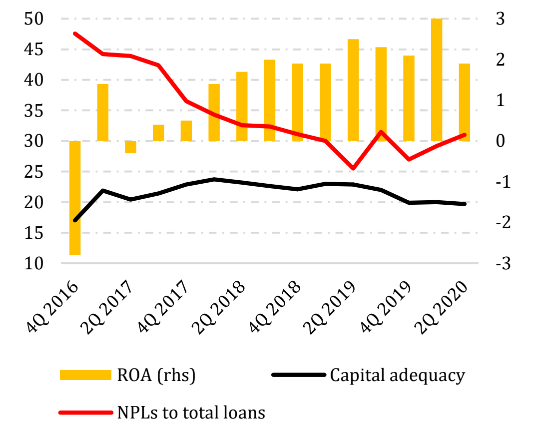
developments and national wealth. Tajikistan is the poorest country in the region with a GDP per capita at USD 3,6 th as of the end of 2019. The Corruption Perception Index stood at 25 (153rd place out of 198 countries) in 2019, the inequality adjusted HDI index was 0,57 in 2018, while unemployment was estimated at 11% in 2019 and heavily exposed to migration flows. Moreover, the country occupied only the 106th position out of 190 countries in the Doing Business 2019 report.

**Debt and deficit expected to widen substantially.** Even before the global economic crisis the growth of debt levels and widening of fiscal deficit were expected due to the needs to finalize several infrastructural projects and high share of FX-denominated debt. The COVID-19 crisis accelerated this trend. The decline in economic activity led to a drop in tax and non-tax revenues, already subdued by the moratorium on tax inspections introduced in 2019 and advance payments, as well as granted exemptions from the VAT. On the expenditures side, additional pressure came from containment measures, health checks at the border, establishment of quarantine zones, and other prophylactic and disinfection actions. Later the government announced the fiscal stimulus plan, which includes among others financial support to SMEs and subsidizing food for the population, as well as time-bound tax holidays and relief to targeted industries and small businesses until 1 September 2020. This is expected to lead to a deficit of up to 7-8% of GDP by end 2020 (see graph 2), while 2021-2022 metrics are subject for monitoring.

The Tajik government has requested disbursement under IMF Rapid Credit Facility instrument and already in May 2020 a disbursement of USD 189,5 m were approved. In addition, further financial support from international organizations, such as the World Bank and the Asian Development Bank is expected. Together with the sharp devaluation of TJS in 1Q 2020 (up to 80% of total public debt is FX), this is expected to lead to a substantial increase of the debt load with debt to GDP and debt to revenues ratios to exceed 50% and 200% by end 2020 respectively and to remain close to these levels in 2021 as well (see graph 3).

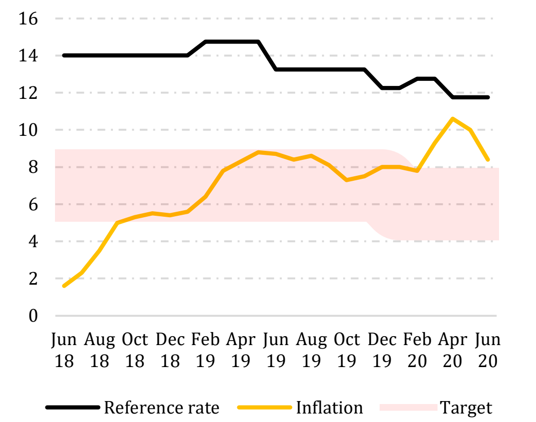
At the same time, the Tajik government confirmed its commitment to the fiscal consolidation after the crisis: authorities agreed on deficit targets of 4,4% of GDP in 2021, and 2,6% of GDP in 2022, and keep debt at manageable levels. We will keep monitor both deficit and debt levels on the recovery stage, taking into account significant needs of investments to finalize infrastructure projects, the lack of internal capacity for revenue growth, as well as large contingent liabilities arising from the high level of indebtedness of unprofitable SOEs, and problems with large banks. However, the debt risks are partially mitigated by the fact that most of the

**Graph 4:** Financial soundness indicators, %



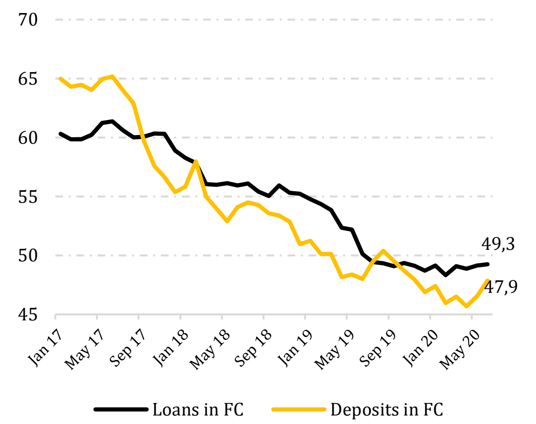

Source: RAEX-Europe calculations based on data from the NBT

**Graph 5:** Reference rate vs inflation rate, %




Source: RAEX-Europe calculations based on data from the NBT

**Graph 6:** Financial dollarization, % of total




Source: RAEX-Europe calculations based on data from the NBT

debt is related to donors support, including IMF, and has concessional terms.

**Gradual deterioration of the banking system metrics is expected.** As we mentioned in our previous report[1], due to strong economic growth and improvement of the bank supervision quality and transparency, the banking industry showed signs of recovering before COVID-19, while problems with two large systemically important banks (Agroinvestbank and Tochiksodirotbank) remained in place. The lock-down measures, turbulence on financial markets, as well as depreciation of TJS in 1Q 2020 led to the deteriorations of banks' metrics. However, the prompt response of the National Bank of Tajikistan (NBT) (see below) smoothed the shocks.

The ratio of NPLs to total loans, as of end 2Q 2020 slightly increased up to 31% of total loans. The banking sector' profitability remains positive despite gradual decline: as of end of 2Q 2020, ROE and ROA amounted to 7,0% and 1,9%, respectively. Capitalization in the system remains adequate as the capital adequacy ratio remained high at 19,7% (see graph 4).

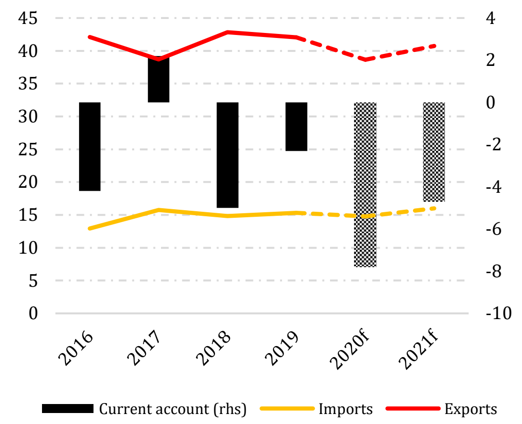
Taking into account the high share of FX-loans (up to 50% by end 2Q 2020), creating risks from unhedged borrowers, we expect further growth of NPLs, as well as decline of capitalization and profitability metrics. In the mid-run, the overall development of the financial system remains subdued, with banks' assets and domestic credit to GDP ratios at 28,4% and 15,8% as of end-2019 respectively, low level of trust of the banking system from population and absence of listed shares currently traded on the national Central Asia Stock Exchange (Dushanbe).

**The NBT showed a prompt response to the economic crisis, while effectiveness of the monetary policy remains limited.** At the beginning of February 2020 the NBT increased its interest rate by 50b.p. up to 12,75%, while also allowing a sharp depreciation of the TJS (by 5% in one month). The latter, together with some local factors, such as food price increase, led to a spike of inflation up to 10,6% by the end of March from 8% at the end of 2019. However, the decline of economic activity and consumption, led to lower inflationary pressures. In April the policy rate was cut by 100b.p. to 11,7% and so far remains unchanged (see graph 5).

In order to support the banking system, the NBT lowered reserve requirements on deposits, relaxed enforcement of prudential requirements and provided foreign exchange liquidity. It also plans to provide emergency liquidity assistance in domestic currency to help ensure financial sector stability in the face of possible deposit outflows from banks.

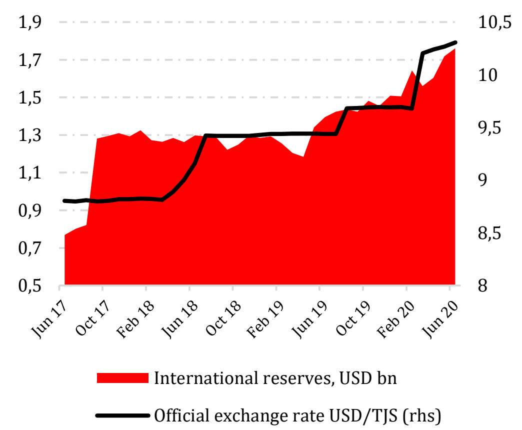
[1] See Research Report on Tajikistan from 7 February 2020: https://www.raexpert.eu/reports/Research_report_Tajikistan_07.02.2020.pdf

**Graph 7:** External sector indicators, % of GDP




Source: RAEX-Europe calculations based on data from the WB, IMF

**Graph 8:** International reserves and exchange rate




Source: RAEX-Europe calculations based on data from the WB, IMF, NBT

Although these measures can be assessed as adequate response to the economic turbulence, in our view, the effectiveness of the monetary policy remains limited by the poor stance of the banking system, undeveloped local capital markets, as well as low independency of the NBT. In addition, despite gradual decline over the last years, the dollarization levels remain high and can increase in the following months (see graph 6), creating distortions for the transmission mechanism. We also expect inflation to be volatile during 2H 2020, but to be close to the upper bound of the NBT's target of 6% (+/- 2p.p.) by end 2020.

**Deterioration of the external position is underway.** The external position of Tajikistan slightly improved by end-2019, but still remained very fragile. The ratios of exports and imports to GDP reached 15,6% and 42,7%, while trade and current account deficits slightly narrowed to 26,7% and 2,3% respectively (see graph 7), on the back of stronger remittances and a significant increase in gold exports. Supported by the NBT's domestic gold purchases, international reserves reached around USD 1,5 bn close to 6 months of imports (see graph 8).

The external trade restriction and sharp drop of remittances inflow (especially from Russia), drastically affected the external position of the country in 1H 2020. The current projections show the current account deficit at around 7-8% of GDP by end 2020, due to a combination of sharply lower remittances and lower non-gold exports. On the other hand, imports are likely to fall substantially due to the closure of the border with China and lower domestic absorption, which will likely lead to a slightly lower trade deficit. In addition, the historically high prices for gold support the exports.

It is worth to mentioning, that according to IMF estimates, without further IMF financing and support from other donors, the reserves would fall significantly to 3,6 months of imports in 2020 or the exchange rate could fall drastically. The FX-currency market remains managed by the NBT and the informal market of FX-currency exists, while the authorities committed to gradually remove the existing currency restrictions by allowing exchange rate flexibility and transit to a fully flexible exchange rate regime by 2023.

**Important note for sovereign ratings**

This Research Report shall be treated as a supplementary part of the published Press Release included in the following link:

https://raexpert.eu/reports/Press_release_Tajikistan_07.08.2020.pdf

Both documents shall be treated as essential parts of each other.

For further information on the factors, their weights, methodologies, risks and limitations of these ratings, and other regulatory disclosures, please refer to the Press Release and the website of the Agency.