

## 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 revised IMF estimations stood at around 11% of GDP and 30% of budget revenues in 2015 and remain the lowest among Uzbekistan's regional peers<sup>1</sup>;
- Historically low short-term debt continues to have a positive impact on the rating<sup>2</sup>. The maximum amount between 1997 and 2013 would be as low as 1% of the projected GDP for 2015;
- FX reserves remain solid covering gross government debt by more than 3x and representing around 40% of GDP;
- Fiscal balance was estimated by the IMF at 0,9% of GDP in 2015. However, it is expected to continue to narrow due to an increase in government spending;
- Real GDP growth grew around 8% in 2015. However, due to regional spillovers (causing remittances to fall sharply and exports to decline) and low commodities' prices, growth is expected to decline sharply in 2016;
- NPLs (0,4% of total loans in 2015) and capital to assets ratio (11,2% in 2015) remain solid in the banking sector according to data from the World Bank;
- Significant amount of natural resources (mainly natural gas, gold and cotton).

#### Restricting factors:

- Fiscal policy is focused on spending to sustain growth and in October 2016 a new increase in wages, allowances and pension benefits will come into effect. This, among other factors, is projected to bring the fiscal balance to a deficit in 2016;
- Government debt, according to the IMF, is estimated to increase substantially in 2016 up to 16% due to the loose fiscal stance;
- The Central Bank has sustained the reference rate at 9% since it trimmed it from 10% in January 2015. This reflects a loose monetary policy while inflation remains high.

<sup>1</sup> Regional peers include Armenia, Azerbaijan, Belarus, Georgia, Kazakhstan, Kyrgyzstan, Russia and Tajikistan.

<sup>2</sup> Total outstanding short-term debt from 1997 to 2013 provided by the Asian Development Bank.

#### Negative factors:

- Uzbekistan remains one of the most undeveloped countries in the region as shown by the low level of GDP per capita (estimated at USD 6 068 by the IMF in 2015) and HDI index of 0,57;
- Inflation, according to IMF figures, has remained high but steady (estimated at 8,4% in 2015<sup>3</sup>). However, inflationary pressures have started to mount due to the uncertainty after Islam Karimov's death;
- The unemployment rate, as reported by the World Bank, was as high as 10,6% in 2014. However, it has exhibited stability in the past years;
- The volume of bank assets increased by around 13% in 1H 2016, compared to 16% from 2014 to 2015 in absolute terms showing a faster pace in credit growth. The adjusted figure for 2015 showed bank assets to GDP at 38% still reflecting limited levels of credit;
- Sluggish institutional development with low transparency and quality of official statistics and high levels of corruption in the country (ranked 153<sup>rd</sup> out of 167 countries in 2015 according to Transparency International). These factors may harm the political transition the country currently faces;
- The share of state-owned banks in the banking system remains substantially high (about 80% of total bank assets at end-2014). Nevertheless, the major SOBs remain strong and stable with low NPLs and acceptable levels of liquidity;
- Underdeveloped financial system with 316 listed companies on the national stock exchange as of September 2016 and market capitalization as low as 5,1% of GDP as of July 2016. Additionally, the ten most active issuers account for 99,6% of the total trades.

#### Stress factors:

- Capital controls leading to currency black markets and other distortions remain a constraint in Uzbekistan. 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 external. Additionally, restrictions to operate in foreign currency, the currency parallel market and the obligation for exporters to surrender a partial or full amount of their FX proceeds constitute the main currency risk of Uzbekistan.

#### ADDITIONAL FACTORS THAT INFLUENCED CCE RATINGS:

##### Negative factors:

- Limited amount of instruments in the financial market;
- Banks' loan policy is harmed by state-directed lending.

##### Restricting factors:

- Low protection of investors as evidenced by the ranking of Doing Business (Uzbekistan ranked 88<sup>th</sup> out of 180 countries in 2015).

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<sup>3</sup> The Central Bank of Uzbekistan (CBU) reported an inflation rate of 5,6% for 2015. The Agency used the IMF estimate for the assessment due to the lack of transparency in the reported statistics.

## SENSITIVITY ASSESSMENT:

The following developments could lead to an upgrade:

- 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 stance (fiscal balance and steep debt increases);
- Economic and political turmoil as a result of a rough transition for the new leader of the government.

“The ratings of Uzbekistan remain constrained by the continued growth of the FX black markets, underdevelopment of the financial markets and institutions, lack of government transparency and a concentrated financial system combined with low credit growth and marginal amount of financial instruments.

Low government debt, narrow fiscal balance and strong GDP growth positively affected the ratings; however, these indicators are set to deteriorate at end-2016 due to higher spending and regional slowdown. Additionally, the high level of international reserves also supported the country’s creditworthiness.

Furthermore, the political transition, albeit smooth at the moment, could cause economic and political instability if the process is not carried in a rigorous manner.” – Clarified Hector Alvarez, Rating Analyst of Rating-Agentur Expert RA GmbH.

Responsible expert: Hector Alvarez, Rating Analyst of Rating-Agentur Expert RA GmbH

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

Research report on Uzbekistan is available at:

[http://raexpert.eu/reports/Research\\_report\\_Uzbekistan\\_23.09.2016.pdf](http://raexpert.eu/reports/Research_report_Uzbekistan_23.09.2016.pdf)

Next scheduled rating publication: TBD in December 2016

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RATING HISTORY:

Date	Review reason	SGC		CCE	
		National currency	Foreign currency	National currency	Foreign currency
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 20 September 2016. 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.

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## 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.