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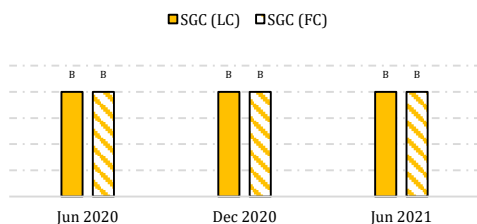
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Ratings

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 Kyrgyzstan

Macro indicators	2018	2019	2020
Gross gov. debt, KGS bn	312	319	407
Nominal GDP, KGS bn	569	619	598
Real GDP growth, %	3,5	4,5	-8,6
Gross gov. debt/GDP, %	54,8	51,6	68,0
Deficit (surplus)/GDP, %	-0,6	-0,1	-3,3
Inflation rate, %	0,5	3,1	9,7
Current Account Balance/GDP, %	-	-	4,5
External debt, USD bn	-	-	4,1
Development indicators	2020		
Inequality adj. HDI	0,63		
GDP per capita, USD th	5,0		

Source: RAEX-Europe calculations based on data from the IMF, WB, Ministry of Finance of the Kyrgyz Republic and NBKR.

RAEX-Europe confirmed at 'B' the credit ratings of Kyrgyzstan. The rating outlook is negative.

RAEX-Europe confirmed the sovereign government credit ratings (SGCs) 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 is negative which means that in the mid-term perspective there is a high probability of downgrading the rating score.

Summary

The ratings of Kyrgyzstan were confirmed at 'B' and the outlook remains negative. The decision mainly reflects the lingering strain on the Kyrgyz economy derived from the coronavirus crisis. As a result of the pandemic, the fiscal position deteriorated, we saw economic contraction and elevated inflation levels. In addition, despite the banking sector having posted acceptable figures, it is expected to show asset quality deterioration as a lagged effect from the crisis.

However, we expect the economy to recover as the world recovers from the pandemic. Nevertheless, the recovery will mostly be dictated by the pace of the worldwide vaccination campaign.

The economy suffered a deep contraction in 2020. Real GDP in Kyrgyzstan posted a negative growth of -8,6% in 2020 mainly as a result of the negative impact from the coronavirus crisis; however, the figure is better than what we anticipated in our previous review. The pandemic caused external demand to drop thus impacting exports, remittances, investments, the gold mining industry, construction, and private consumption. In addition, the border closure with China also affected the country substantially. In 1Q 2021, we saw a continued struggle for positive economic growth. The mining sector remained depressed, while domestic and external demand was weak; moreover, the tourism sector did not recover as the pandemic did not ease as expected.

Nevertheless, we anticipate 2H 2021 to post better figures as the world recovers from the pandemic. However, this will largely depend on the pace of the vaccination campaign worldwide and, especially in Kyrgyzstan. As of 24 June 2021, the Deputy Minister of Health Bakyt Jangaziev reported that only 1,5% of the population had been vaccinated. We expected real GDP to grow at a pace of around 3,8% y-o-y by the end of 2021.

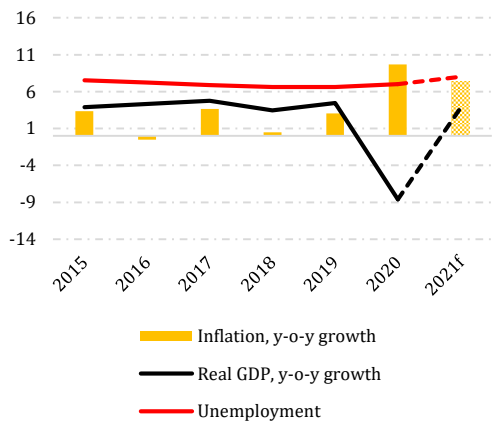
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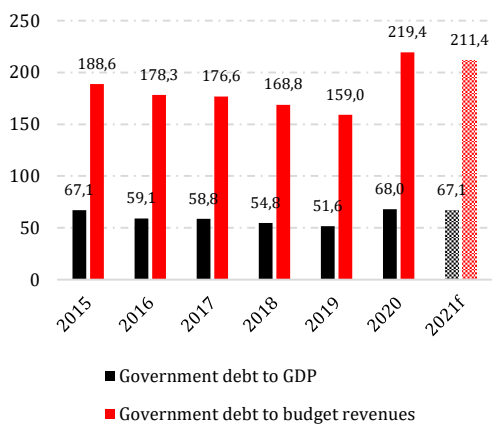
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Graph 1: Macroeconomic indicators, %



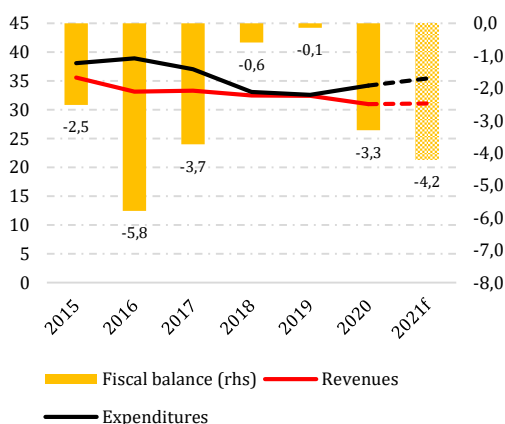
Source: RAEX-Europe calculations based on data from the IMF

Graph 2: Government debt dynamics, %



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

Graph 3: Fiscal budget dynamics, % of GDP



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

Kyrgyzstan remains one of the poorest countries in the Central Asia region with GDP per capita in PPP terms of about USD 5,0 th in 2020. The dependence on the gold output from the Kumtor mine, keeps the Kyrgyz economy concentration risk high.

What is more, the political events which transpired in 2020 led to the resignation of President Sooronbai Jeenbekov and, protesters-supported Sadyr Japarov emerged as interim prime minister and the elected president at the beginning of 2021. We expect parliamentary elections to take place this autumn. All this turmoil and uncertainty is expected to add plenty of political and, thus, economic instability to the country.

Finally, the official level of unemployment was around 7% in 2020, but we consider the real level of unemployment significantly higher since large part of the labor force before the pandemic worked abroad.

Government debt hiked substantially in 2020. As previously anticipated, government debt increased up to 68% of GDP and 219% of budget revenues in 2020. This was chiefly a consequence of increased financing from multilateral and bilateral debt from international institutions, while domestic public debt also increased. Moreover, the depreciation of the KGS against the USD also played an important role in the increase as 87% of the debt is denominated in foreign currency. Despite this, the currency risk is partially mitigated since most of the external debt is at concessional terms. In addition, short-term debt remained low at 0,4% of total debt.

We anticipate government debt levels to remain high in 2021, but to start a declining path going forward. As of April 2021, government debt had only increased by around 2,7% in absolute terms. Finally, the increase on the debt level will also highly depend on a potential renewed devaluation of the KGS against the USD.

Fiscal deficit widened but outlook is better than initially anticipated. The budget deficit stood at 3,3% of GDP in 2020 as revenues were 30,1% of GDP and expenditures posted a figure of 34,2% in 2020. Revenues by around 13% mainly as a result of lower tax collection due to the measures introduced to support the economy. These include postponing tax payments, timing exemptions of property and land taxes, and provisional price controls on some food items, as well as tax exemptions on SMEs. On the other hand, expenditures increased as anti-pandemic measures implemented by the government included support to vulnerable groups, subsidized credits, among others.

We expect the deficit to widen further in 2021 as the government continues to support the economy to fight the negative effects from the pandemic. Moreover, given the high level of government debt and low public buffers, we consider that the authorities do not have substantial room to maneuver in case additional shocks were to occur. However, the

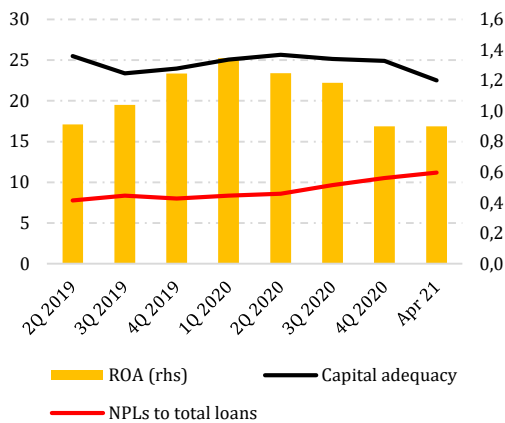
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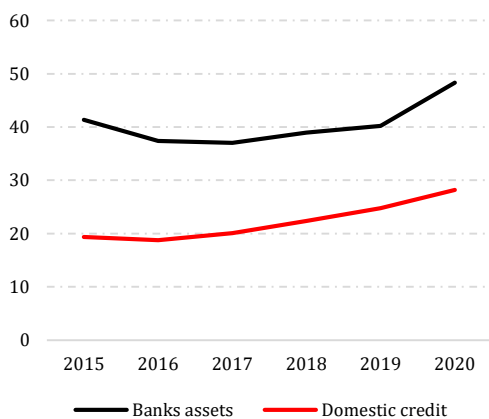
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Graph 4: Financial soundness indicators, %



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

Graph 5: Credit to the economy dynamics, % of GDP



Source: RAEX-Europe calculations based on data from the WB and NBKR

continued availability of concessional funds for the country is a good sign that the support may come again if needed.

Monetary policy transmission remains restricted. The inflation rate increased substantially in 2020 and stood at 9,7% y-o-y resulting from the exchange-rate pass through given the KGS depreciation, as Kyrgyzstan is an economy extremely dependent on imports. In addition, the metric has continued to rise in 2021 and it posted a reading of 10,9% y-o-y as of May 2021, way above the National Bank of the Kyrgyz Republic (NBKR) target of 5%-7%. The above has caused the NBKR to increase the policy rate twice in 2021. In February 2021, the rate was increased from 5% to 5,5%, while in April the hike was more aggressive as it went up to 6,5% as the increase in food prices does not appear to ease. We expect inflation to remain high and volatile within the following years as it highly depends on external factors

In addition, as mentioned in our previous review, the NBKR has taken important steps to improve monetary policy transmission and predictability. One of the actions taken to improve this was narrowing the boundaries of the interest rate corridor. Despite this, levels of financial dollarization remained high, which continues to hamper the effectiveness of the monetary policy. As of April 2021, the share of FX deposits in total deposits stood at 45,4%, while the share of FX loans was 31,3%. We anticipate the effectiveness of the monetary policy to remain limited by elevated dollarization levels.

The banking sector has remained resilient but expected to worsen. The banking system has showed health in the past year as most financial soundness indicators have been favorable; however, it is already showing signs of slight deterioration. As of April 2021, the capital adequacy ratio stood at 22,5%, showing a decline of around 2p.p. as compared to year-end 2020. The level of NPLs to total loans ratio increased from 10,5% at the end of 2020, up to 11,2% in April 2021. This metric has been steadily increasing for the past two years. On the other hand, profitability has remained practically unchanged in the past four months as ROA and ROE posted figures of 0,9% and 5,9% respectively.

The adequate metrics were mostly a result of the measures adopted by the NBKR to ease the strain of the pandemic on the banking sector and the economy. These measures were mostly about postponing the application of several regulatory requirements in terms of liquidity, reserves, and capital adequacy, among others. However, despite the acceptable figures, we might see some lagged effects due to new problem loans kicking in after the pandemic as a consequence of loan payment deferrals. Also, we could observe liquidity and capital adequacy deterioration as the asset weighting comes back to normal.

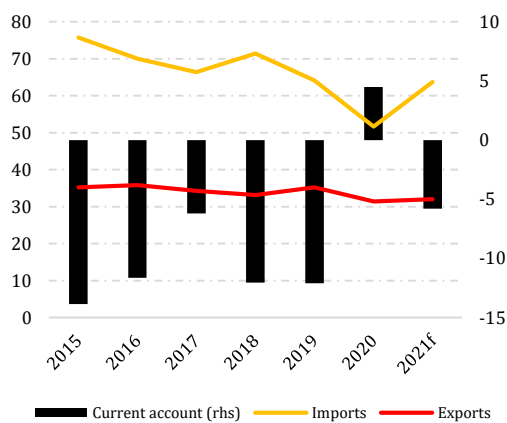
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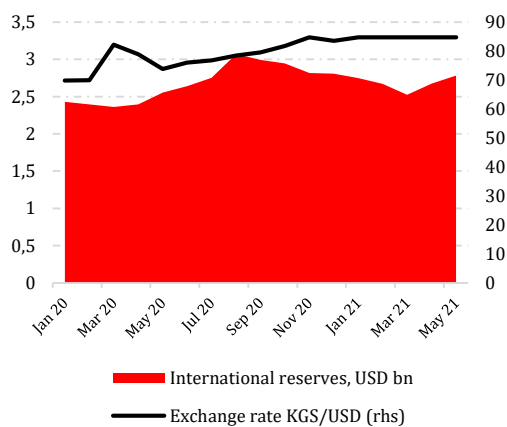
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Graph 6: External sector indicators, % of GDP



Source: RAEX-Europe calculations based on data from the IMF and NBKR

Graph 7: International reserves and exchange rate



Source: RAEX-Europe calculations based on data from the IMF and NBKR

Banks assets to GDP increased by 8p.p. up to 48,4% as cash started pile up in the banks' accounts in the form of deposits and corresponding accounts, while credit grew slightly. Domestic credit provided by the banking sector increased up to 28,2% of GDP in 2021, 4p.p. higher than in 2020. However, the relative increase was mostly propelled by the contraction of nominal GDP.

External position remains weak. In 2020, imports declined by 29,7% y-o-y as a result of the temporary cross border closure with China due to the pandemic, combined with lower domestic demand. On the other hand, the reduction in external demand during the peak of the coronavirus crisis, led to a decline in exports of around 22,2% y-o-y. The strong drop in imports caused the trade deficit to narrow down to 22,2% of GDP. However, the stability of current transfers reflected a positive current account of 4,5%. We do not anticipate this trend to continue in 2021 as we expect imports to grow substantially, while exports to do so at a moderate pace. This will result in a renewed negative current account balance of about -5,6% of GDP by year-end.

The decline in the trade deficit was accompanied by turbulence on the global financial markets and increased geopolitical risks in the region. As a result, by mid-November, the KGS weakened against the USD by 22% since the beginning of the year but has remained fairly stable so far in 2021. In order to smooth out sharp corrections in the exchange rate, the NBRK intervened in the FX market. At the same time, the level of international reserves remains stable at USD 2,78 bn as of May 2021.

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, 31,3% of total loans and 45,4% of total deposits were denominated in foreign currency (very weak stress-factor).

SENSITIVITY ASSESSMENT:

The following developments could lead to an upgrade:

- Significant decline of external government debt;
- 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;

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- 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.

Next scheduled rating publication: 17 December 2021. The full sovereign rating calendar can be found at [Sovereign Rating Calendar 2021](#)

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RATING HISTORY:

Date	Review reason	SGC		Outlook	
		National currency	Foreign currency	National currency	Foreign currency
18.12.2020	Scheduled revision of both types of ratings for the country	B	B	Negative	Negative
26.06.2020	Scheduled revision of both types of ratings for the country	B	B	Negative	Negative
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

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Minute's summary

The rating committee for Kyrgyzstan was held on 25 June 2021. 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 August 2020). 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.

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Office responsible for preparing the rating

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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.

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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.

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