

5 March 2021

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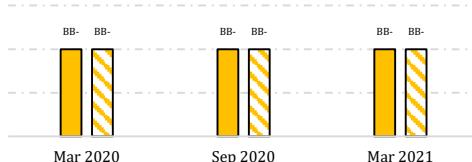
Ratings

Sovereign Government Credit (LC)	BB-
Sovereign Government Credit (FC)	BB-
Outlook (LC)	Stable
Outlook (FC)	Stable

* These ratings are unsolicited

Ratings dynamics

■ SGC (LC) □ SGC (FC)



Main Economic Indicators of Uzbekistan

Macro indicators	2018	2019	2020*
Gross gov. debt, LC bn	118335	150050	216140
Nominal GDP, LC bn	406649	511838	598206
Real GDP growth, %	5,4	5,6	1,6
Gross gov. debt/GDP, %	29,1	29,3	36,1
Overall fiscal Deficit (surplus)/GDP, %	-2,3	-3,9	-5,6
Inflation rate, %	14,3	15,2	12,1
Current Account Balance/GDP, %	-	-	-9,6
External debt, USD bn	-	-	22,8
Development indicators	2020		
Inequality adj. HDI	0,72**		
GDP per capita, USD th	7,2		
Default indicator	05.03.2021		
9Y Gov Bond Yield***, %	3,1		

Source: RAEX-Europe calculations based on data from the IMF, WB, CBU, NSC.
*Estimation **2019 ***Government bonds with remaining maturity 9 years

RAEX-Europe has confirmed at 'BB-' the ratings of Uzbekistan. The rating outlook is stable.

RAEX-Europe has confirmed the sovereign government credit ratings (SGC) of Uzbekistan at 'BB-' (Sufficient level of creditworthiness of the government) in national currency and at 'BB-' (Sufficient level of creditworthiness of the government) in foreign currency. The rating outlook is stable, which means that in the mid-term perspective there is a high probability of maintaining the rating score.

Summary

The confirmation of Uzbekistan's ratings at 'BB-' with stable outlook reflects the acceptable level of public debt and decent economic performance amid the COVID-19 pandemic. The economy of Uzbekistan remains actively developing and the government remains committed to continuing the ongoing structural reforms. In addition to that, the banking sector remains stable with adequate profitability and capitalization levels. However, in the context of the persisting pandemic, augmented social spending might continue, which could require additional government borrowing. The explicit effects of the pandemic are still to be observed and will depend on the speed of COVID-19 vaccination rollout in Uzbekistan and worldwide and the consecutive pick-up or stagnation of business activity.

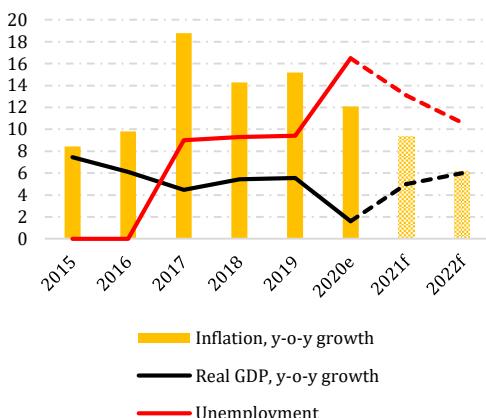
The ratings remain restrained by high inflation, low levels of institutional development and national welfare, and elevated levels of unemployment. Furthermore, despite improved management and transparency, the effectiveness of the monetary policy is undermined by the heavy segmentation of bank lending, high financial dollarization and underdeveloped local capital markets.

As expected, the COVID-19 pandemic has had a significant impact on economic growth in 2020. Uzbekistan has faced lower external demand due to sluggish economic activity globally, as well as lower private consumption and investment, caused by quarantine restrictions and uncertainty. Despite the significant impact of the pandemic, Uzbekistan is one of the few countries able to avoid economic contraction in 2020, showing a year-end GDP growth of 1,5%. With the rollout of the vaccination, relaxation of the lockdown measures and the pick-up of

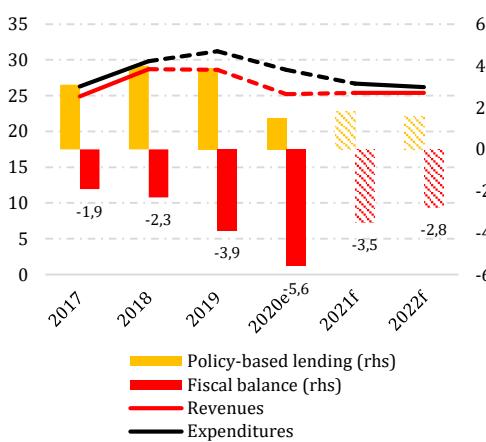
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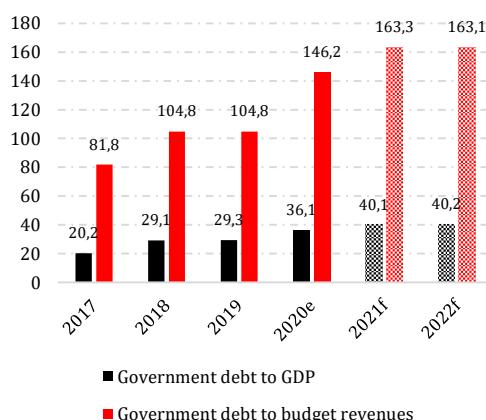
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Graph 1: Macroeconomic indicators, %


Source: RAEX-Europe calculations based on data from the IMF, WB, State Committee of the Republic of Uzbekistan on Statistics, Ministry of finance of the Republic of Uzbekistan

Graph 2: Fiscal budget dynamics, % of GDP


Source: RAEX-Europe calculations based on data from the IMF and WB *Overall fiscal balance in IMF definition, that includes policy-based lending

Graph 3: Government debt dynamics, %


Source: RAEX-Europe calculations based on data from the Ministry of finance of the Republic of Uzbekistan

economic activity we expect the growth rate of the economy to come back to its pre-pandemic levels of 5-6% in the medium term (see graph 1). Our base case scenario can however be restricted by the introduction of new lockdown measures and the issues with the rollout of the vaccines.

Since a large share of the country's labor force works abroad and due to the contraction of the main labor markets for Uzbekistan, namely Russia and Kazakhstan, the rate of unemployment has increased to 16,5% in 2020 (9,3% in 2019) and remains one of the main restricting factors. With the pick-up of economic activity in Uzbekistan and abroad, we expect the unemployment rate to decrease to 13% in 2021 and reach the levels of 9-10% in subsequent periods (see graph 1). Additionally, GDP per capita in PPP terms remains very low among regional peers¹ (USD 7,2 th in 2020).

Fiscal position has worsened due to additional expenses in response to COVID-19. Although the budget revenues remained resilient in 2020, due to the urgent need to cushion the effects of the COVID-19 pandemic the government had to increase spending on social sphere and medical care which has contributed to the widening of the overall fiscal deficit² to 5,6% by the end of 2020 (see graph 2). Provided that the pandemic will be kept under control and additional COVID-19 expenditures will not be required, we expect the fiscal balance to return to its pre-pandemic levels in mid-term perspective (see graph 2).

Going forward we see two main factors which will define the stability of Uzbekistan's public finances in the mid-term: the development of the situation with COVID-19 and the continuation of the government's reforms regarding improvements in fiscal planning and transparency, reduction of the volume of policy lending, and implementation of announced plans for privatization of the massive public sector.

Despite the growth, the level of public debt to GDP remains at an acceptable level. Uzbekistan's total public and publicly guaranteed (PPG) debt increased to 36,1% of GDP as of 2020 (see graph 3), compared to 29,3% of GDP in 2019. The growth of public debt in 2020 was associated with the attraction of external borrowings to finance additional budget expenditures to combat the negative consequences of the COVID-19 pandemic and for further financing of state economic development programs. At the expense of concessional loans from the international financial institutions, the Anti-Crisis Fund was created. Despite the growth, Uzbekistan's public debt remains moderate and does not add additional risks to the country's creditworthiness. Moreover, we highlight the favorable maturity structure of the public debt, with 95% of the debt

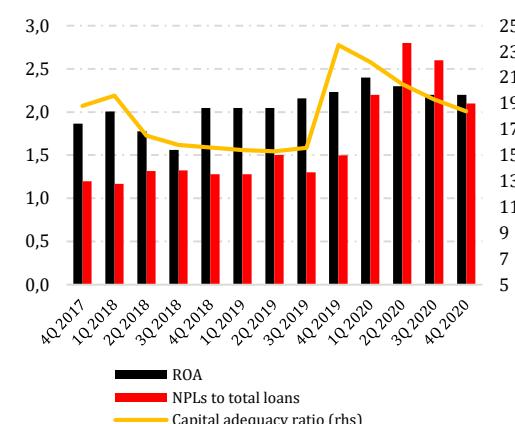
¹ Here Caucasus and Central Asia (CCA) oil and gas exporters: Azerbaijan, Kazakhstan, Turkmenistan, and Uzbekistan.

² Includes policy-lending operations in IMF definition.

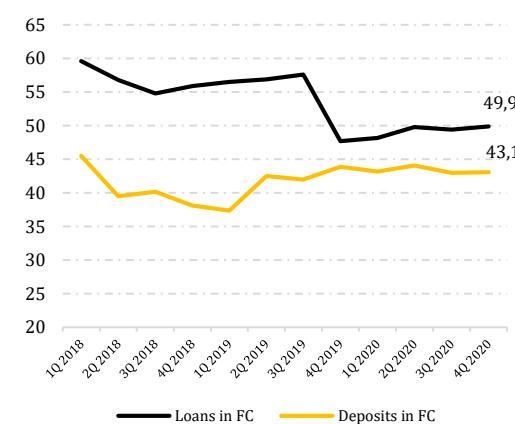
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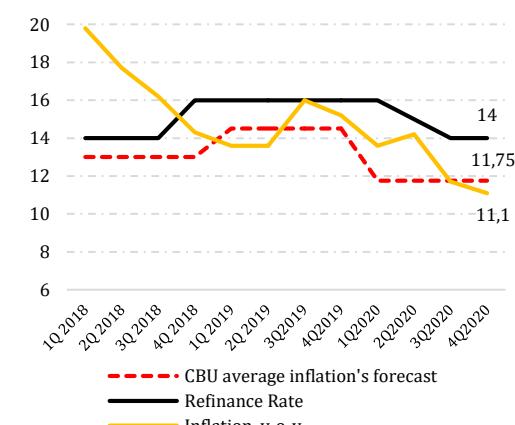
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Graph 4: Financial soundness indicators, %


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

Graph 5: Financial dollarization, % of total


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

Graph 6: Refinance rate vs inflation rate, %


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

maturing in more than one year and 83% of debt maturing in more than five years. We also highlight the fact the majority of the debt comes in form of concession agreements with foreign governments and state banks, as well as international financial institutions. In terms of currency structure, the prevalence of foreign currency-denominated debt (99% of debt) remains a key risk factor, making the debt position vulnerable to currency fluctuations. After a sharp devaluation of UZS in April 2020, the national currency has continued to weaken through the end of 2020 and beginning of 2021, which will increase the debt burden. Although the government seeks to diversify debt structure by issuing domestic bonds, their share remains insignificant, and further issuance of these instruments is limited by the underdeveloped domestic capital market. In addition, we continue to note the high level of contingent liabilities of the government related to SOE and SOB debts, which may be lowered as the implementation of the privatization program continues.

Banking sector remains resilient despite the challenges of COVID-19.

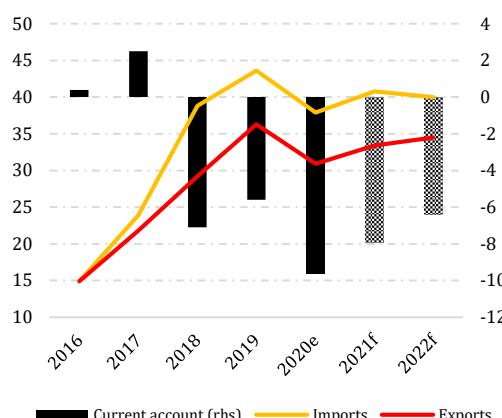
The banking sector has remained stable throughout 2020, despite the destructive impact of COVID-19. After observing an increase in the share of NPLs in the first half of 2020, the share of NPLs has consecutively lowered in 3Q and 4Q and reached the level of 2,2% by the end of 2020 (see graph 4). The profitability of the banking sector has remained stable during 2020, with ROA being at the pre-pandemic level of 2,2% at the end of 4Q. We note the timeliness of the Central Bank of Uzbekistan (CBU) precautionary measures to ensure financial stability and to maintain adequate liquidity of commercial banks. The regulator makes use of REPO and swap operations; it has reduced reserve requirements and introduced a special credit line to provide liquidity to banks for up to three years. The ratios of banking system assets and domestic loans to GDP, while both showed growth in 2020, remain at moderate levels of 61,2% and 46,3% respectively at the end of 2020. The role of the financial sector for the economy is limited due to the high concentration of assets on state-owned banks (85% of sector's assets in 2020), as well as a still significant share of preferential loans to public sector enterprises. We expect a reduction of systemic risks of the banking sector if the authorities' plans to cancel policy lending to SOEs at below market rates are executed.

Monetary policy has contributed to the provision of macroeconomic stability. The CBU has implemented a set of measures in order to support the economy during the pandemic which included postponement of repayment of loans to the population and businesses, maintaining the liquidity of the banking system and ensuring the stability of the payment system. Given the impact of the pandemic on the macroeconomic situation

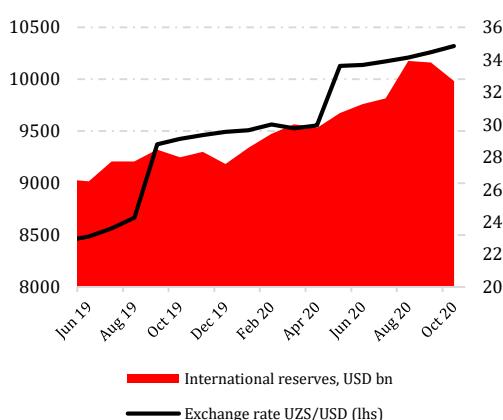
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Graph 7: External sector indicators, % of GDP


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

Graph 8: International reserves vs exchange rate


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

Stress or Support factors:

- The level of financial dollarization of the economy remains high. At the end of 4Q 2020, the share of FX in total deposits and loans was 43,1% and 49,9% respectively.

SENSITIVITY ASSESSMENT:

The following developments could lead to an upgrade:

- Faster than expected recovery of the global economy, which can lead to an improvement of the external position of Uzbekistan and to enhance the state of government finances;
- Smooth continuation of the initiated structural reforms of the public business sector with reduction of the government footprint in the economy and banking industry;
- Further improvement of the exchange-rate flexibility and monetary policy, providing more freedom to monetary authorities, resulting in a long-term and controlled reduction of inflation and levels of financial dollarization.

The following developments could lead to a downgrade:

- Continued lock-down measures in the country and longer period of turbulence in the global economy, which would lead to further deterioration of the external position, as well as a contraction of local economy;

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and the dynamic of the inflation the CBU reduced the key rate to 15% in April, and further to 14% in September (see graph 6).

Overall, the CBU continues to improve the quality, predictability and transparency of its monetary policy within the framework of inflation targeting and the transition to a free-floating exchange rate regime. The regulator maintains its course to achieve the inflation target of 10% in 2021 and 5% by 2023. A number of factors however, including an increased level of financial dollarization (see graph 5) and underdeveloped domestic capital markets, limit the effectiveness of the monetary policy transmission mechanism.

The current account deficit in 2020 has widened to 9,6% of GDP (see graph 7). However, we expect this reading to narrow in 2021 as the economic activity picks up and the amount of export and remittances increases. As of October 2020, the international reserves amounted to USD 32,7 bn, covering 12 months of imports (see graph 8).

- Deterioration of the stance of the banking system, which would materialize contingent liabilities of the government;
- Higher than expected increase of the government debt and deficit metrics due to the need of additional financing for the government expenditures, and underperforming of tax and external revenues.

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 and droughts have negative 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**.

Next scheduled rating publication: 3 September 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
04.09.2020	Scheduled revision of both types of ratings for the country	BB-	BB-	Stable	Stable
06.03.2020	Scheduled revision of both types of ratings for the country	BB-	BB-	Stable	Stable
06.09.2019	Scheduled revision of both types of ratings for the country	BB-	BB-	Stable	Stable
08.03.2019	Scheduled revision of both types of ratings for the country	BB-	BB-	Stable	Stable
14.09.2018	Scheduled revision of both types of ratings for the country	B+	B+	Positive	Positive
16.03.2018	Scheduled revision of both types of ratings for the country	B+	B	NA	NA
22.09.2017	Scheduled revision of both types of ratings for the country	B+	B	NA	NA
24.03.2017	Scheduled revision of both types of ratings for the country	B+	B	NA	NA
23.09.2016	Scheduled revision of both types of ratings for the country	B+	B	NA	NA
15.04.2016	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 Uzbekistan was held on 5 March 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, 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), Asian development bank, Ministry of Finance of Uzbekistan, Transparency International.

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.

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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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