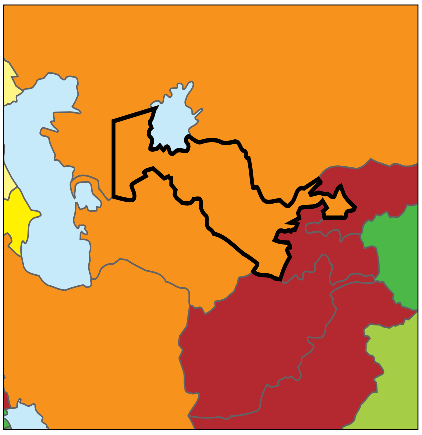
14/06/2017

6/7 COUNTRY RISK CLASSIFICATION

COUNTRY RISK CLASSIFICATION
Uzbekistan

0 1 2 3 4 5 6 7

The country risk classifications are on a scale of 0 to 7.
The lower the number, the better the credit rating.



CONTACT

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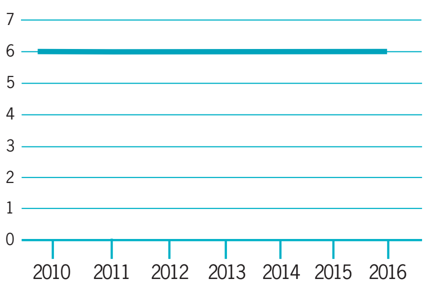
BASIC FACTS

Population	31 million (2016)
Nominal GDP	USD 67 billion (2016)
GDP/capita	USD 2 161 (2016)

COUNTRY CLASSIFICATION HISTORY



Source: EKN

Cautious improvement after the power shift in Uzbekistan

President Karimov, who has been in power since the country's independence in 1991, passed away in September 2016. Fears of a potential power vacuum were not realised, and in December former prime minister Mirziyoyev rose to the presidency.

Economically, the past decade has been characterised by high economic growth, increased diversification of the economy and a constant increase in the international reserves. Politically and institutionally, however, the development has been considerably slower. The country is relatively isolated from the rest of the world, the state's involvement in the economy is extensive, and the regulatory environment is very complicated. Other risk factors are the economy's raw material dependency and its strong connections to Russia. President Mirziyoyev has initiated economic reforms but extensive and speedy changes are unlikely. The country's current economic and political situation is thereby not expected to change in any material aspects.

EKN places Uzbekistan in country risk classification 6 of 7. Normal risk assessment is applied in general, but with certain exceptions. EKN has limited experience of covering payment risks in Uzbekistan.

THE COUNTRY'S STRENGTHS AND WEAKNESSES

STRENGTHS

+ Large international reserves and low debt level.
+ Considerable raw material supply.
+ High growth and a relatively diversified economy.

WEAKNESSES

- Political uncertainty with a breeding ground for domestic and regional conflicts.
- Extensive state involvement in the economy and strict foreign exchange regulations inhibit entrepreneurship, trade and investment.
- Very weak regulatory environment with widespread corruption and politicised judicial system.

SWEDISH EXPORT TO THE COUNTRY, MSEK

Uzbekistan	MSEK
2016	160
2015	154
2014	146
2013	478
2012	186

Source: Statistics Sweden

EKN'S EXPOSURE

	MSEK
Guarantees	986
Offers	0

EKN'S POLICY

Uzbekistan has had country risk classification 6 of 7 since 2008, a classification which is determined in consultation with OECD. EKN can cover state risks, but for other public purchasers, a letter of credit or bank or state guarantee is required.
Normal risk assessment is applied in the event of bank and corporate risks. Due to foreign exchange regulations, the waiting period for claims adjustment in the event of non-payment is extended.

EKN'S EXPOSURE AND EXPERIENCE

EKN's experience of issuing guarantees to purchasers in Uzbekistan is limited, and somewhat negative. In several cases, companies have lost necessary licences or had their operations expropriated by the state. In addition, company employees have been imprisoned and the potential to recover equipment has proven to be low. EKN's commitment is currently dominated by a guarantee within the gas sector.

WHAT MIGHT CAUSE A CHANGE IN THE COUNTRY POLICY

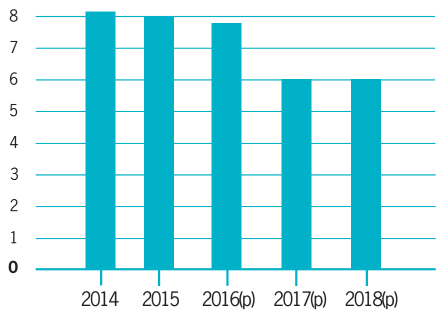
EASING

- A clear improvement of the business environment, including the politicised judicial system, high corruption levels and strict foreign currency regulations.
- A stabilisation of the domestic political situation and improved relationships with neighbouring countries.

TIGHTENING

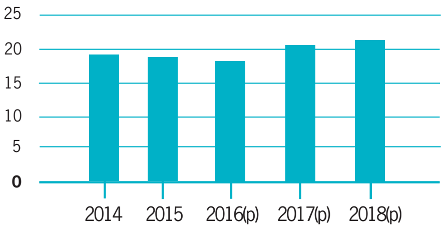
- Drastic deterioration of commodity revenues and declining economic growth.
- Drastic increase in debt level and depletion of the international reserves.

GDP-GROWTH (% PER ANNUM)



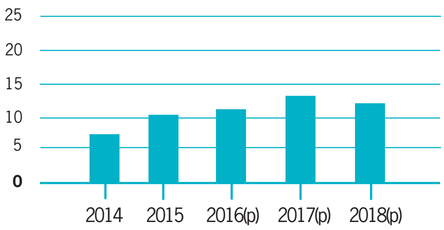
Growth shows a declining trend.
Source: IMF WEO 2017

INTERNATIONAL RESERVES (MONTHS OF IMPORT)



Uzbekistan's international reserves is large and growing.
Source: IMF REO 2017

PUBLIC DEBT (% OF GDP)



The public debt is low in relation to GDP.
Source: IMF REO 2017

COUNTRY ANALYSIS

BACKGROUND

Since its independence in 1991, Uzbekistan's political situation has been formed by ex-president Islam Karimov's rule. In autumn 2016, the country underwent its first power shift since the independence as former prime minister Mirziyoyev rose to the presidency following an election without any real opposition candidates, thereby avoiding the feared power vacuum with potential social unrest as a consequence. The new president has demonstrated a cautious willingness to reform, primarily with regard to the economy and the country's foreign policy.

MOST RECENT TRENDS

A proposal for a liberalised foreign exchange policy in 2017 has been put forward. Among other things, it concludes reliefs with regard to currency conversion, and in January the president established four new free economic zones. On the foreign policy level, Mirziyoyev has showed signs of being more internationally-minded than his predecessor. Steps have been taken to improve relations with neighbouring countries. In April 2017, for example, the flight route between Tashkent and Dushanbe (Tajikistan) was opened, which until this point had been closed for 24 years. Improved relations with neighbours are welcome as this means a lower risk of war and a potential increase in trade. Uzbekistan has water conflicts with Kirghistan and Tajikistan, and there have long been tensions in the Fergana Valley. With hope for a better situation in terms of human rights under Mirziyoyev, the EBRD has decided to re-open its office in Tashkent which closed in 2007. Once in place, EBRD will likely work to promote wider economic reforms.

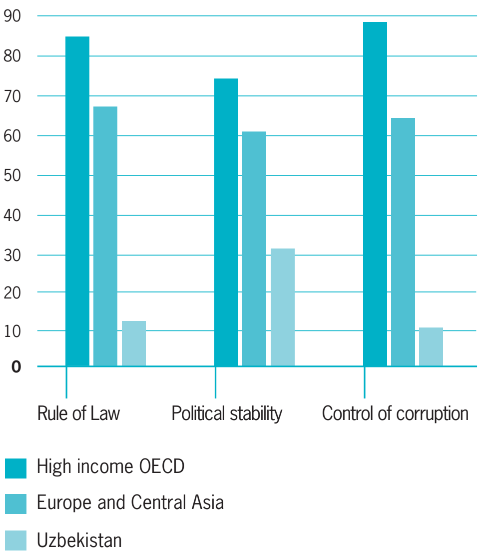
Extensive and speedy political and economic reforms are however unlikely. Mirziyoyev was prime minister under Karimov for 13 years and has strong ties to the former regime. There is therefore uncertainty surrounding just how strong the new presidents willingness to reform really is. The capacity to achieve change is limited by the possibility to implement reforms without jeopardising social security in the country and challenging powerful interests. Under Karimov's strong control over governance and the security forces, social unrest could largely be stifled. By lifting the lid, Mirziyoyev risks national discontent over the authoritarian rule, corruption, and high inflation. There is potential for conflict between the country's clans, opposition groups and militant Islamists in the country.

GDP growth has been very strong over the past decade; on average over eight per cent. The negative economic development in Russia during the period 2014-2016 affected Uzbekistan through a decrease in remittances from Uzbek guest workers in Russia and through a decreased demand for natural gas and cars. Overall, however, the Uzbek economy proved resistant to the declining Russian economy. Surpluses in public and external finances combined with low indebtedness facilitated increased public consumption and contributed to the GDP growth holding steady at around eight per cent throughout the period. Since 2014, gold production has increased, which has meant that gold is the largest export product and Switzerland the largest export destination ahead of China, Turkey and Kazakhstan (2015). Russia continues to be an important export market, primarily for cotton yarn and clothing. Relations with Russia have been frosty at times, which is linked to Uzbekistan's unwillingness to allow itself to be affected by foreign powers, and the country has thus far chosen to stand outside of Russia's customs union (EAEU). Closer relations with Russia are however likely in the coming years and discussions regarding future membership may be considered.

LONG-TERM TRENDS

A gradual decrease in the growth rate is expected in the long term. Uzbekistan's closed and centrally planned economic model will inhibit the productivity needed in order to maintain high growth and reduce raw materials dependency. The state controls large parts of the economy in a manner reminiscent of the command economy structures of the Soviet era. Since the early 2000s, Uzbekistan has had a surplus in its current account due to its the considerable exports raw materials. Cotton, natural gas and gold together constitute half of the export. Considerable oil and gas reserves constitute a potential for increased export and investments in the future. Both the weak regulatory environment and the judicial system are hindrances and foreign direct investments are relatively low. The external debt has decreased steadily over the past decade and amounted to around 16 per cent of GDP whilst the debt service ratio is very low. The international reserves have increased considerably during the same period and corresponds to close to 18 months' import coverage. The central bank's policy for protecting the domestic industry, supporting export and reinforcing the international reserves has led to a falling exchange rate. At the same time, the policy entails high import prices, which has contributed to the high inflation of around ten per cent. The exchange rate is officially floating, but in practice bound to the US Dollar via a crawling peg, which means that it is allowed to depreciate gradually. On the black market, the Uzbekistani Som is traded at roughly half the official rate and is at risk of falling drastically if the proposed easing with regard to currency conversion becomes a reality. This would lead to a marked increase in inflation and further depletion of households' purchasing power, which may have a negative impact on social stability in the country.

BUSINESS ENVIRONMENT



Ranking from 0 (worst) to 100 (best)

Source: World Bank

BUSINESS ENVIRONMENT

The business environment in Uzbekistan is among the weakest in the world. The state's involvement in the economy is considerable. Overseas companies' business opportunities are dependent on their relations with the state or state-owned companies. Regulations can change quickly, licences can be withdrawn and operations expropriated, which in recent years has taken place in the mining, trade and telecom sectors, among others. Corruption is widespread, and Uzbekistan is ranked 156 of 176 countries in Transparency International's Corruption Perceptions Index. In the World Bank's ranking of countries' corporate climate, the country ranks 87 of 189, which is a marked improvement compared with the period prior to 2013. Among other things, it has become easier to register new companies and handle bankruptcies, whilst at the same time customs regulations have been simplified. The overall regulatory environment remains very weak, however. The legal system is inefficient and politicised and suffers from a lack of predictability.

The banking sector is small and concentrated, and is dominated by the state. The country's largest bank – the state-owned National Bank of Uzbekistan – has a market share of over 20 per cent. The banking sector's loan as a proportion of GDP is low; around 20 per cent, but is growing. The banking system is relatively well capitalised and credit losses are low overall. As the systemically important banks are state-owned, the likelihood of support from the state in the event of a banking crisis is high. The banks' credit rating is thereby strongly linked to the condition of state finances and can quickly deteriorate in the event of a crisis in these finances or the external position.

Companies' accounting primarily follows local standards whilst the banks largely fulfil the requirements laid down in IFRS. The lack of access to financing and foreign currency makes matters difficult for companies. A protectionist policy is applied, in which investments in export sectors are stimulated whilst imports are kept down. The strict capital controls are intended to minimise the capital outflow, regulate imports and stimulate local manufacturing. Conversion from local to foreign currency can take from three months to over a year. The import of intermediate goods and raw materials is therefore very time consuming and costly. There are also requirements imposed on companies to convert 50 per cent of foreign exchange proceeds to local currency.
The private sector's access to foreign currency is very limited overall, which runs the risk of leading to delayed payment from Uzbek importers.