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## **IMF Executive Board Concludes Article IV Consultation with the Republic of Tajikistan**

On April 21, 2009, the Executive Board of the International Monetary Fund (IMF) concluded the 2009 Article IV consultation with Tajikistan.<sup>1</sup>

### **Background**

Economic developments in 2008 were favorable, despite a severe winter, a prolonged drought, and electricity shortages. Real GDP growth reached 8 percent in 2008, mainly driven by remittance-financed demand in the services and construction sectors, and non-cotton agricultural production. Inflation receded from its mid-2008 peak, to 11 percent year-on-year in February 2009. With strong domestic demand, the trade balance worsened in 2008. Imports grew by around 36 percent, reflecting high international food and energy prices in the first half of the year, while exports were held back by sluggish industrial activity. Despite this, the overall balance of payments registered a surplus in 2008 as remittances surged by 50 percent.

The authorities completed their June–December 2008 staff-monitoring program. The government achieved an overall fiscal surplus (excluding externally financed investment) of 1 percent of GDP, higher than targeted under the program, and mainly driven by buoyant revenues. The associated build-up of government deposits at the National Bank of Tajikistan (NBT) helped the NBT contain reserve money growth, while accumulating international reserves at a faster pace than envisaged. Gross international reserves stood at \$228 million at end-2008, equivalent to 1.3 month of imports.

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<sup>1</sup> Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities.

In 2009, Tajikistan faces a negative external shock that is aggravated by domestic problems. With the global slowdown—in particular in Russia—remittances are projected to decline by 30 percent in 2009. Moreover, exports (mainly cotton and aluminum) are projected to contract by 7 percent in value terms. This will require a large balance of payments adjustment, which will be accompanied by weaker demand. On the supply side, ongoing electricity rationing and expected water shortages during the agricultural season are weighing on growth. As such, real GDP growth is projected to decline to 2 percent at best. Inflation should stabilize around 13 percent in 2009.

Tajikistan's financial system remains vulnerable, despite improvements in some financial soundness indicators during 2008. Some banks face severe funding problems due to large corporates drawing down their deposits, a drying up of trade credits and advances for remittances, and rising nonperforming loans. Moreover, the economic slowdown is expected to deteriorate asset quality in 2009, and somoni depreciation could further add to the stress in the banking sector. In response, most banks have started to raise deposit rates and have constrained credit growth. In addition, the NBT has provided liquidity loans, mainly in somoni.

### **Executive Board Assessment**

Executive Directors agreed with the thrust of the staff appraisal. They welcomed the good economic performance in 2008, but observed that Tajikistan is facing a severe external shock from the global economic crisis, the effects of which are compounded by domestic rigidities. Tajikistan is likely to be affected in particular by the serious regional downturn, which could lead to a decline in remittance inflows, putting pressure on the external position and threatening the livelihoods of many poor households that depend on remittances for basic income. Weakening external demand is depressing the main exports—cotton and aluminum—further worsening the external position. Continued heavy state influence over markets and poor energy infrastructure put prospects for faster growth at risk. Poverty remains widespread, and could increase as the economic outlook deteriorates.

Against that background, Directors agreed that macroeconomic policies should be geared toward maintaining external stability. They supported the planned restrained fiscal stance, while commending the authorities for raising critical social expenditures. They called on the authorities to fund only those investment projects that are likely to enhance growth prospects. They welcomed the authorities' commitment to tighten policies in the event of a prolonged or more severe global economic downturn.

Directors commended the authorities for improving tax revenues and maintaining fiscal discipline under the staff-monitored program, which has contributed to a further reduction in debt. They encouraged the authorities to rely exclusively on concessional financing in the period ahead to avoid a renewed buildup of unsustainable debt. They welcomed that the National Bank of Tajikistan (NBT) had begun to rebuild international reserves in 2008.

Directors generally welcomed the authorities' commitment to a flexible exchange rate regime, which will help to contain the external current account deficit and support adjustment to external shocks. They took note of the staff assessment that the real effective exchange rate of the somoni could be overvalued. They endorsed the authorities' intention to reduce excess volatility in the foreign exchange market.

Directors observed that although the banking sector has not yet been affected by the global financial crisis, it remains vulnerable, including through its exposure to the cotton sector and deteriorating asset quality. They encouraged the authorities to move quickly to strengthen the liquidity management framework, and with contingency plans to deal with distressed institutions. Supervision should also be enhanced, and steps taken to ensure that banks adhere to regulatory standards.

Directors endorsed the authorities' structural reform agenda. They stressed the need to push forward with agricultural sector reforms to remove rigidities and secure macroeconomic stability and growth. Efforts will also be needed to enhance transparency and accountability in state-owned enterprises.

Directors welcomed the publication of the executive summary of the special audit of the NBT as evidence of improved transparency and governance. They emphasized the crucial importance of swift and comprehensive implementation of the audit recommendations.

It is expected that the next Article IV consultation with Tajikistan will be held in accordance with the Executive Board decision on the consultation cycle for members with Fund arrangements.

**Public Information Notices (PINs)** form part of the IMF's efforts to promote transparency of the IMF's views and analysis of economic developments and policies. With the consent of the country (or countries) concerned, PINs are issued after Executive Board discussions of Article IV consultations with member countries, of its surveillance of developments at the regional level, of post-program monitoring, and of ex post assessments of member countries with longer-term program engagements. PINs are also issued after Executive Board discussions of general policy matters, unless otherwise decided by the Executive Board in a particular case.

## Republic of Tajikistan: Selected Economic Indicators, 2005–09

	2005	2006	2007	2008	2009
	Act.	Act.	Act.	Act.	Proj.
Production and prices	(Annual change in percent)				
Real GDP	6.7	7.0	7.8	7.9	2.0
CPI inflation (period average)	7.3	10.0	13.2	20.4	12.4
General Government	(In percent of GDP)				
Total Revenue and grants	20.1	23.6	21.6	21.3	21.0
Of which: grants	0.7	4.7	1.1	0.8	1.9
Expenditure and net lending	23.0	21.9	27.8	27.5	27.9
Of which: social expenditure <sup>1/</sup>	...	...	7.5	7.3	8.7
Of which: capital expenditure <sup>2/</sup>	7.8	6.8	14.1	13.9	10.6
Overall balance <sup>3/</sup>					
Excluding externally financed investment	0.5	0.8	1.6	1.3	-0.5
Including externally financed investment	-3.1	1.7	-6.2	-6.2	-7.0
Monetary Indicators	(Annual change in percent, unless otherwise indicated)				
Broad money	30.2	63.4	78.8	6.3	8.3
Velocity of broad money (end-of-period)	7.7	6.1	4.7	6.1	6.8
External sector	(In million of U.S. dollar, unless otherwise indicated)				
Exports of goods and services <sup>4/</sup>	601	656	767	814	756
Imports of goods and services <sup>4/</sup>	1,221	1,618	2,555	3,469	2,792
Current account balance	-62	-79	-414	-453	-522
In percent of GDP	-2.7	-2.8	-11.2	-8.8	-9.7
Gross official reserves <sup>5/</sup>	91	111	107	199	228
In months of next year's imports <sup>6/</sup>	0.9	0.7	0.5	1.2	1.3

Source: Tajik authorities; and Fund staff projections.

1/ Includes current and capital spending on social protection, education and health.

2/ Includes domestically and externally financed investments.

3/ 2006 overall balance excludes the Multilateral Debt Relief Initiative that is reflected in grants.

4/ Starting in 2005, the export and import figures reflect the transition to tolling arrangement for aluminum.

5/ Gross reserves are net of the pledged deposits of the NBT.

6/ Excludes electricity, which is on barter basis, and imports for projects financed with loans from China.