



Tajikistan

The Russian financial crisis, the deterioration in terms of trade, and adverse weather have slowed Tajikistan's economic recovery. Redoubled efforts in privatization and structural reforms, as well as continued commitment to the peace process, are necessary to promote economic growth and prosperity.

RECENT TRENDS AND PROSPECTS

Since its civil war ended in 1997, Tajikistan has made significant progress in creating a stable macroeconomic environment and implementing market-oriented reforms. However, economic growth slowed in 1999 with real GDP growing 3.7 percent (see figure 2.5). This decrease reflects the adverse effects of the Russian financial crisis, the deterioration in Tajikistan's terms of trade, and adverse weather.

Agriculture is a key sector of the economy, contributing 20 percent to GDP and accounting for 60 percent of employment. Agricultural production increased by 3.8 percent in 1999, but production of cotton (the country's most important cash crop) and grain fell by 17.6 and 20 percent, respectively, because of bad weather and limited financing. Industrial production grew 5 percent in 1999, led by aluminum, electricity, and wood and timber. Production of aluminum, the major export, increased 20 percent.

The official unemployment rate was 3.1 percent in 1999, but actual unemployment was close to 30 percent. The official data do not account for unemploy-

ment and underemployment in inactive state-owned enterprises and rural areas. Moreover, many of the unemployed have not registered because of the low unemployment benefits.

Budget overruns and weak tax administration widened the budget deficit during the first three quarters of 1999. However, the authorities intensified revenue collection and rationalized expenditures in the fourth quarter. As a result, the deficit fell to 3.1 percent of GDP in 1999 after a 3.8 percent deficit the previous year. The deficit is being financed by concessional borrowing from multilateral lending institutions, privatization proceeds, and an issue of Treasury bills.

The Russian financial crisis damaged Tajikistan's economy. After enjoying more than a year of hard-won stability, the official exchange rate of the Tajik ruble against the dollar depreciated 47.5 percent from August 1998 to August 1999. Since then, however, the exchange rate has remained stable, and will likely depreciate more gradually as the Russian economy improves.

Since June 1997, the authorities have pursued a tight monetary policy to reduce inflation, which fell

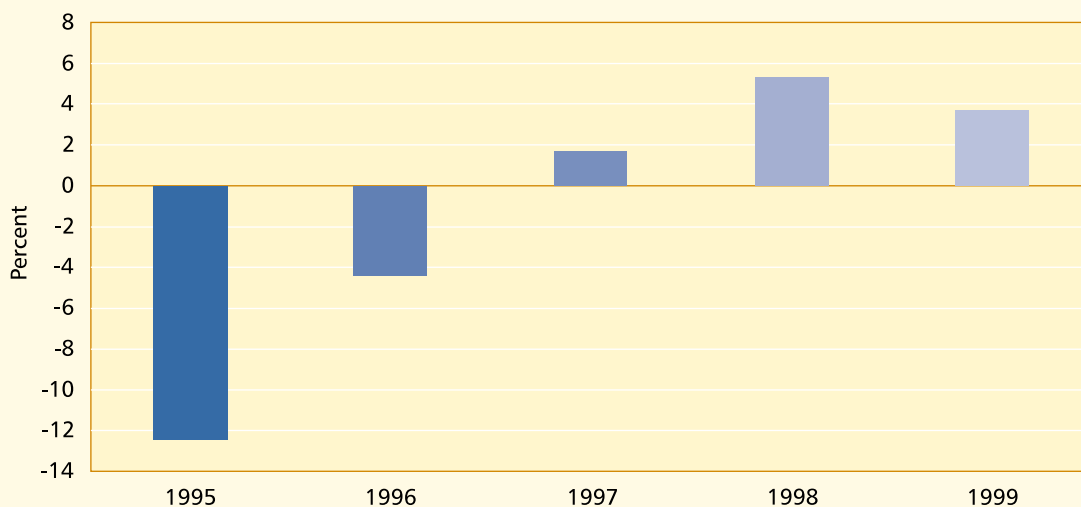
from 159.8 percent in 1997 to 2.7 percent in 1998. However, the currency devaluation between August 1998 and August 1999 renewed inflationary pressures. Tajikistan faced more shocks in 1999 when prices of key commodities increased. In August, fuel prices rose 50 percent and bread prices 20 percent as the effects of the low grain harvest began to manifest themselves. Administrative price increases in electricity and gasoline also contributed to inflation, which increased to 24 percent in 1999.

Tajikistan continued its liberal trade regime in 1999. In 1998, a uniform tariff of 5 percent was levied on most major imports. In February 1999, Tajikistan joined the customs union of the Commonwealth of Independent States, and raised its average tariff rate to 8 percent. However, the government remains committed to a liberal trade regime and announced that it will apply for World Trade Organization membership, emphasizing that it will not introduce trade policies that violate the organization's policies.

The trade balance faces substantial instability because of the lack of diversity in exports and the volatility in their prices. More than three fourths of export earnings come from cotton and aluminum. In 1998, the trade balance deteriorated sharply when world market prices for both of these products decreased, but recovered in 1999 when the price of aluminum rebounded. Export earnings from aluminum increased 36 percent, although earnings from cotton declined 18 percent as cotton's price continued to fall. The appreciation of the Tajik ruble against the Russian ruble after the Russian crisis caused decreased exports to former Soviet countries in 1999. However, diversifying trading partners since independence cushioned the effects of the crisis. For example, Tajikistan sells cotton and aluminum mostly to countries that were not in the former Soviet Union.

The debt-service burden continues to be heavy. In April 1999, however, Russia agreed to reduce Tajikistan's debt more than 50 percent. Agreements

**Figure 2.5 Real GDP Growth Rates,
Tajikistan, 1995-1999**



Source: ADB (2000).

were also signed with Kazakhstan, Kyrgyz Republic, Turkey, and Uzbekistan. The European Union, India, and Pakistan also indicated a willingness to reschedule Tajikistan's debt. Consequently, the foreign debt service fell from \$181 million (34.4 percent of exports) in 1996 to \$29 million (7.6 percent of exports) in 1999. However, because of the currency depreciation, the debt-to-GDP ratio increased from 91.4 percent in 1998 to 97.2 percent in 1999.

POLICY AND DEVELOPMENT ISSUES

Continued progress in the peace process is the most crucial factor in maintaining a stable macroeconomic environment that will foster economic development and promote investor confidence.

The peace process made significant progress in 1999. The United Tajik Opposition announced in August 1999 that it had completed disarming opposition fighters and integrating them into the Tajik armed forces. The United Tajik Opposition emphasized that it is no longer an armed opposition, but only a political opposition. The Supreme Court subsequently lifted the 1993 ban on opposition parties. Security conditions also improved in much of the country. However, the presidential election in November was criticized by domestic and international observers for irregularities and strained relations between the government and the opposition.

Only 35 percent of recorded GDP is generated in the private sector. However, privatization of small enterprises accelerated in 1999, and in December, the government announced that its privatization program for small enterprises was complete. Moreover, by September 1999, half of state and collective farms had been dismantled, 45 percent of arable land was in private hands, and 63,000 marketable land share certificates were distributed to individual farmers. Privatization of medium and large state-owned enterprises lagged, however, and only seven of 23 cotton gin mills had been sold by October 1999. Problems included unrealistic pricing by the government and delayed payments by buyers. The government has also been slow in restructuring the two largest firms—the electricity monopoly Barki Tajik and the aluminum smelter TADAZ.

The banking sector has performed poorly since 1991 because of weak management skills, directed credits, an inadequate legal and regulatory framework, and a background of political and macroeconomic instability. Consequently, a large proportion of bank loans is nonperforming. Confidence in the banking sector is diminished, which keeps deposits low and severely limits commercial credit expansion. Given the importance of this sector, the authorities are restructuring it.

The first round of restructuring was completed in November 1998, and progress was made in reducing bank staff, improving management practices, and expanding the capital base. In 1999, new prudential regulations reduced the number of banks from 26 to 16, as several weak banks were liquidated or merged with other banks. In April 1999, the National Bank of Tajikistan, the central bank, took over one of the big five banks to liquidate it because of noncompliance with prudential regulations, an action that should set an important example for other banks.

Agricultural finance has been especially constrained in recent years. Financing for the newly privatized "peasant farms" is virtually nonexistent, as the current rural finance system is not designed to accommodate them. Consequently, farmers have been forced either to borrow from moneylenders, enter into forward contracts with suppliers and traders at unfavorable terms, or limit production. The need to develop sustainable rural financial institutions is crucial.

Because of the sharp economic contraction since independence, the government's ability to provide basic social services has been severely strained, and the estimated poverty rate is 83 percent. Although the political and economic situation has stabilized somewhat since 1997, the Russian financial crisis and the deterioration in Tajikistan's terms of trade in 1998 and 1999 have exacerbated fragile living conditions. In the past two years, the country was also hit by major floods that destroyed or damaged infrastructure, homes, and crops. However, the existing social safety net remains inadequate and poorly targeted. With a high incidence of poverty and the government's limited resources, the need to reform and strengthen the social safety net is urgent.