

Tajikistan

Winter energy shortages failed to derail another year of strong growth, but structurally the country faces difficult economic and social conditions, including a high poverty rate, an unfavorable investment climate, and weak infrastructure. In the short term, growth will be affected by the global—and especially regional—slowdown. A continued, heavy fall in workers' remittances, a major source of family income and foreign exchange, is a major risk. The country is facing the adverse impact of the global financial crisis and economic downturn, and the Government and donors are making efforts to mitigate economic losses.

Economic performance

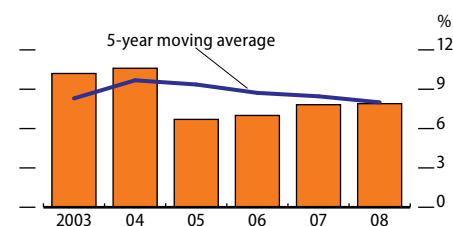
In 2008, the economy posted solid growth estimated at 7.9%, despite a decline in industrial production and contraction in the key aluminum and cotton subsectors (Figure 3.6.1).

Industrial production as a whole declined by 4% in 2008. Including aluminum production, industry was hit by an energy crisis (and subsequent power rationing) that was triggered by an unusually cold winter in 2008. This lowered the water level in the country's largest reservoir below that needed for generating normal hydropower supplies. Among three important subindustries that had been major drivers of industrial growth in 2007—food processing, construction materials, and textiles—only food processing posted any growth, of just 0.6%. The authorities ensured that this subindustry was less affected by the rationing because of its strategic importance.

Agriculture picked up to 7.9% growth in 2008 from 6.5%, supported by robust expansion in noncotton subsectors, including livestock and fruits and vegetables, as higher global prices made food production more profitable. The area planted to cotton was reduced further in 2008, allowing farmers to grow other crops. The cotton subsector continued to suffer from low productivity, a legacy of heavy debt and a sluggish pace of structural reform. Services rapidly expanded, boosted by strong performance in the construction, trade, and finance subsectors. Construction activity was buoyed by large disbursements on externally and internally financed infrastructure projects. The strong expansion in services offset the decline in industrial production.

Growth in consumption and investment supported expansion in aggregate demand; the contribution of net exports was negative, as imports continued to expand faster than exports. Growth in consumption was heavily supported by remittances, which were estimated at about half of GDP in 2008, up from below two fifths in 2007. Investment growth was underpinned by foreign direct investment inflows and official development assistance, largely for financing infrastructure projects.

3.6.1 GDP growth



Sources: State Statistical Committee of the Republic of Tajikistan, available: <http://www.stat.tj>, downloaded 27 February 2009; staff estimates.

[Click here for figure data](#)

Inflation fell to 11.9% in December 2008 from 19.9% a year earlier (Figure 3.6.2), though the average annual rate remained relatively high at 20.7%. Wheat was a major driver, due to a global price spike and the sizable weight of wheat products in the consumer price index basket. In the last quarter, the retreat in international food prices, and the removal of a wheat export ban from Kazakhstan, helped bring wheat and other food prices down. (Most of the country's food and energy needs, including wheat, are met through imports.)

Utility prices, including natural gas and electricity, also jumped in 2008, owing to higher prices for imported natural gas from Uzbekistan and a hike in electricity tariffs. Fuel prices did not immediately decline with the retreat in international oil prices in the last quarter of 2008, because lower prices were not fully passed through due to rigidities in the domestic market, such as small market size, few importers, and slow inventory adjustment.

A surge in remittances created pressures for the local currency, the somoni, to appreciate in the first half of 2008. To counter them, the National Bank of Tajikistan (NBT) bought foreign exchange to build its low international reserves and to forestall a loss in competitiveness. The nominal exchange rate was kept broadly stable at around TJS3.43/\$1 throughout the year (Figure 3.6.3). Remittances grew at an estimated 50% in 2008, though receipts showed a marked slowing in the fourth quarter.

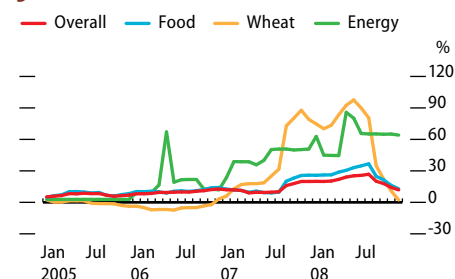
NBT refrained from providing direct credit to the economy, helping lower reserve money growth to an estimated 27%, from 40.3% in 2007. Broad money growth is estimated at about 33.1% in 2008, compared to 78.8% in 2007, as growth in credit slowed.

Revenue and expenditure, excluding the externally financed portion of the Public Investment Program (PIP), are estimated at 20.9% and 19.9% of GDP, respectively, in 2008. The Government achieved the 1% fiscal surplus, due to stronger revenue performance stemming from high nominal growth, improved tax administration, and increased imports.

Including the externally financed portion of the PIP, expenditure was estimated at 28.5% of GDP and revenue at 21.4% (a deficit of 7.2% of GDP) (Figure 3.6.4). Current spending and net lending came in at 15.4% of GDP, including wages and salaries (of 4.3% of GDP). Capital expenditure (13.8% of GDP) comprised externally financed PIP (9.3%) and domestically financed spending (4.5%). Disbursements of the PIP exceeded the planned program as projects moved faster than anticipated.

The current account deficit is estimated to have narrowed to 9.3% of GDP in 2008 from 11.2% in 2007 (Figure 3.6.5), a reflection of the gain in workers' remittances, prompted in part by the jump in domestic food and energy prices. The growth of remittances slowed in the last quarter, as the global slowdown increasingly affected the Russian Federation (the main source of remittances) and Kazakhstan. Although import growth decelerated relative to 2007, imports were about seven times the size of exports. The financing of the heavy trade deficit (and the smaller services and income deficit) was fully dependent on remittance transfers and capital inflows. Import growth was driven largely by goods for household consumption and by construction materials for infrastructure projects. Gross official reserves at year-end are estimated at \$169 million (Figure 3.6.6), equivalent to about 1 month of imports in 2008.

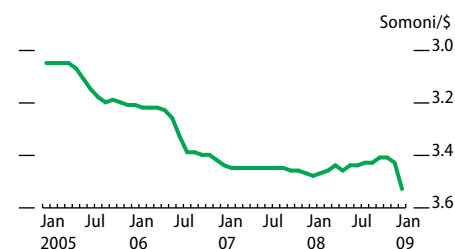
3.6.2 Inflation



Source: State Statistical Committee of the Republic of Tajikistan, available: <http://www.stat.tj>, downloaded 2 February 2009.

[Click here for figure data](#)

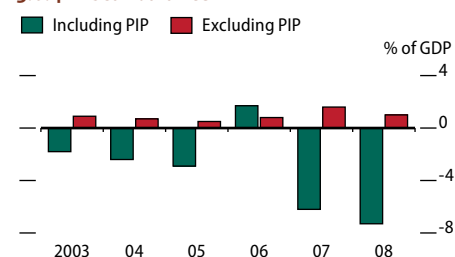
3.6.3 Exchange rate



Source: International Monetary Fund, *International Financial Statistics* online database, downloaded 4 March 2009.

[Click here for figure data](#)

3.6.4 Fiscal balance



PIP = Public Investment Program.

Source: International Monetary Fund, *Country Report* Nos. 07/144 and 08/382, available: <http://www.imf.org/external/country/TJK/index.htm>.

[Click here for figure data](#)

Energy has been attracting significant investment in recent years, through a combination of significant indigenous hydropower potential, growing demand (especially foreign) for energy, and a domestic energy infrastructure degraded by many years of underinvestment. To complement the investment, the Government has started implementing reforms to improve the economic viability and management of the sector. Electricity prices are being raised to cost-recovery levels, as part of which the tariff for the public was virtually doubled to 2 cents per kilowatt-hour at the start of 2009. To cushion the impact, the Government has allocated a budget for the poor and other vulnerable groups.

The slow pace of reform in agriculture, including cotton, and the cotton debt problem are impeding growth. Some moves were made in 2008, though. A decree was adopted that abolishes cotton export licensing by NBT. Also, to enhance transparency, the cotton subsector was financed through a new mechanism, whereby the Government provided funds at low interest rates through commercial banks. However, the mechanism is unsustainable as collecting loan repayments from indebted cotton sector farmers will remain very difficult for commercial banks. The decline in global cotton prices, low productivity, and inefficient cotton ginning and marketing are heavy burdens on the subsector.

The Government made good progress on the Staff-Monitored Program of the International Monetary Fund (IMF). It also adopted a new 3-year debt management strategy, which sets the limit of new public external borrowing in line with the IMF–World Bank Debt Sustainability Analysis (published in March 2007) at 40% of GDP. External debt is estimated at 30% in 2008 (Figure 3.6.7).

Public financial management received attention in 2008. In accordance with the IMF Staff-Monitored Program, a special audit of NBT was conducted, and the Government issued a decree establishing a supervision unit in the Ministry of Finance for regular monitoring of the financial operations of the 10 largest state enterprises.

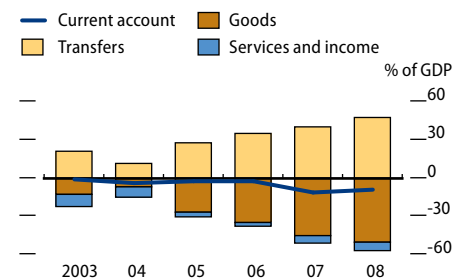
Economic prospects

The external environment—particularly in the Russian Federation—will be extremely demanding in 2009. Falling remittances and sluggish exports will weaken the external balance. Remittances are projected to go down by about 30% this year, possibly more, and were already down by about 22% in January, year on year. The liquidity problems in the banking system may create disincentives for migrants to use it as a channel for making transfers, thus risking losses in an important source of foreign exchange and disruption in formal economic activity. Export earnings will decline due to both price and volume effects stemming from lower demand for aluminum and cotton. World prices, including oil and food, are expected to fall, easing import costs; natural gas import prices, though, will stay high.

Monetary policy will aim to tighten money growth. NBT will not provide direct credits to banks or the economy; growth in reserve money will come from the Government as it draws down its deposits at NBT to finance part of the budget deficit.

Real GDP growth is forecast to fall in 2009 to 3.0%, reflecting the

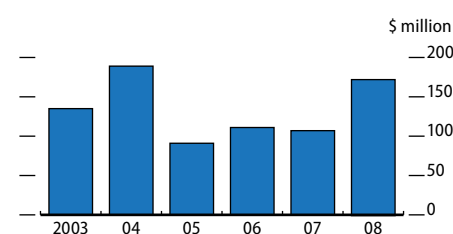
3.6.5 Current account indicators



Source: International Monetary Fund, *Country Report* Nos. 07/144 and 08/382, available: <http://www.imf.org/external/country/TJK/index.htm>.

[Click here for figure data](#)

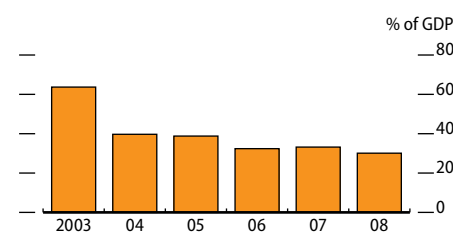
3.6.6 Gross international reserves



Sources: International Monetary Fund, *Country Report* Nos. 07/144 and 08/382, available: <http://www.imf.org/external/country/TJK/index.htm>; National Bank of Tajikistan.

[Click here for figure data](#)

3.6.7 External debt



Source: International Monetary Fund, *Country Report* Nos. 07/144 and 08/382, available: <http://www.imf.org/external/country/TJK/index.htm>.

[Click here for figure data](#)

3.6.1 Selected economic indicators (%)

	2009	2010
GDP growth	3.0	4.0
Inflation	15.5	9.5
Current account balance (share of GDP)	-8.8	-7.0

Source: Staff estimates.

global slowdown. Services growth, the main driver in recent years, will decelerate as remittances decline and credit dries up. The financial system will have difficulties in increasing lending to the economy due to tighter monetary policy and liquidity shortages in the system. Lower international prices and demand for aluminum, as well as weaker domestic spending, will keep industry a drag on growth. Agriculture, though, is expected to continue expanding on favorable supply and demand factors.

Noncotton agriculture, which was a growth driver in 2008, should benefit from the loans allocated from the budget through banks and from a further reduction in the cotton-planted area. Moreover, consumers are expected to switch from imported food to domestically produced food, due to the impact of falling remittances on incomes and prices.

On the expenditure side, lower remittances will slow consumption and consumption-related imports. Investment, however, is expected to grow within the framework of the budgeted infrastructure-related capital spending.

The economy is expected to pick up slightly in 2010 to 4.0%, as new hydropower plants become operational, which will limit energy shortfalls and boost exports. The pickup also depends on some recovery in the global economy and the availability of funding, particularly external private capital and development assistance.

Macroeconomic stability is the major objective of the authorities' economic program. The Government is revising its 2009 budget to reflect the expected impact of worsening economic conditions on revenue collection, and has budgeted a targeted 0.5% of GDP deficit in 2009 (excluding the externally financed portion of the PIP). The budget allocated large increases for health and education, and apportioned funds for lending to agriculture through commercial banks. However, as revenue performance has substantial downside risks, expenditure items will likely need to be revised down, but planned social sector spending may well be maintained. The global donor community is providing support for the financing gap of 2009; additional funding will almost certainly be needed.

Inflation is expected to ease to 15.5% this year and to 9.5% next year, helped by trends in global food and energy prices and weaker domestic demand. Food and energy items are the main determinants of inflation in Tajikistan, given their large weight in the consumer price index basket. The slowdown in the domestic economy and declining remittances will reduce demand-pull pressures.

The current account deficit is projected at 8.8% of GDP in 2009 and 7.0% in 2010. Imports of capital goods related to ongoing PIP projects will be the major driver of the current account deficit and will mirror the fiscal deficits. Consumer goods imports will continue to be covered by remittances, though imports of consumer goods will remain relatively high until savings are depleted. External developments will probably keep export growth essentially stagnant in 2009, with a modest increase in 2010.

The major downside risk to economic prospects in over the forecast period will be the depth of the global and regional recessions. If remittances tumble, this will further damp economic activity and lead to greater external adjustment.

3.6.1 Development challenges

Strategies that the Government adopted at the start of the millennium envisaged a graduation to managing a long-term development process, from the crisis management strategies of the 1990s when the country suffered from civil conflict, macroeconomic instability, and food insecurity. The past year, however, has demonstrated the recurrent fragility of the economy to crises, forcing the Government both to manage the crisis while guiding longer-term strategies.

Remittance dependency has been growing in recent years, reflecting sluggish domestic production and export growth, and some one third of the labor force now works abroad. Although the financial inflows have supported growth and spending, the human outflows have created shortages of labor for certain skills (and disincentives for other family members to work at home).

Managing this dependency is difficult. Employment of returning migrants relies on local job creation, the pace of which in turn hinges on private sector development. And although the Government has started to improve the investment climate for private business where it can by spending more on physical infrastructure, some limitations, such as geography, are immutable.