

**Republic of Tajikistan: 2006 Article IV Consultation—Staff Report; Public Information Notice on the Executive Board Discussion; and Statement by the Executive Director for the Republic of Tajikistan**

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2006 Article IV consultation with the Republic of Tajikistan, the following documents have been released and are included in this package:

- the staff report for the 2006 Article IV consultation, prepared by a staff team of the IMF, following discussions that ended on February 1, 2007, with the officials of the Republic of Tajikistan on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on March 7, 2007. The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF;
- a Public Information Notice (PIN) summarizing the views of the Executive Board as expressed during its March 28, 2007 discussion of the staff report that concluded the Article IV consultation; and
- a statement by the Executive Director for the Republic of Tajikistan.

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INTERNATIONAL MONETARY FUND

REPUBLIC OF TAJIKISTAN

**Staff Report for the 2006 Article IV Consultation**

Prepared by the Middle East and Central Asia Department  
(in consultation with other departments)

Approved by David Owen and Mark Plant

March 7, 2007

**Mission dates:** October 20–November 3, 2006, and January 25–February 1, 2007, at which time discussions on a possible PSI-supported program also took place.

**Team:** C. Piñerúa (head), S. Çakır, M. Sumlinski, S. Vtyurina (all MCD), A. Unigovskaya (PDR), and L. Moers (resident representative).

**Key Tajik officials:** President Rakhmonov, State Economic Advisor Davlatov, Minister of Finance Nadjmiddinov, and National Bank of Tajikistan Chairman Alimardonov.

**Exchange system:** Tajikistan accepted the obligations of Article VIII, Sections 2, 3, and 4 with effect from December 9, 2004 and maintains an exchange system that is free of restrictions on the making of payments and transfers for current international transactions.

**Fund relations:** On February 6, 2006, the Executive Board completed the sixth and final review of Tajikistan's second three-year PRGF arrangement and discussed the Ex Post Assessment of Tajikistan's Longer-Term Program Engagement (EPA). Earlier, the Executive Board had approved debt relief for Tajikistan under the Multilateral Debt Relief Initiative (MDRI) in the amount of SDR 69 million. As of end-February 2007, outstanding obligations to the Fund amounted to SDR 29.4 million (33.8 percent of quota).

**Outreach:** The mission met with members of parliament and held press briefings. It also met with local representatives of the Asian Development Bank, the World Bank, EBRD, UNDP, and briefed members of the diplomatic community. The resident representative's office launched a new website ([www.imf.org/external/country/tjk/rr](http://www.imf.org/external/country/tjk/rr)).

**Data:** Goskomstat (<http://www.stat.tj/>), National Bank of Tajikistan (<http://www.nbt.tj/>) Ministry of Economy and Trade (<http://www.met.tj/>). Despite some weaknesses, data provision is adequate for surveillance. Tajikistan participates in the GDDS.

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## Executive Summary

### Background

**While the recent strong growth performance continued in 2006, inflation accelerated.**

Despite considerable disruptions to energy supply late in the year, real GDP growth reached 7 percent, fueled by a surge in construction activity and continuing strong remittance-financed demand for retail and trade services. However, CPI-inflation reached 12.7 percent, its highest level since 2003, mostly as a result of failed harvests and higher gas prices, but also reflecting a relatively loose monetary policy stance and remittance-related demand pressures. The exchange rate has been relatively stable, with reduced intervention in the foreign exchange market.

**Inflation risks for 2007 are on the upside, mostly because of the recent decision by Uzbekistan to double gas export prices.** While staff welcomed the authorities' decision to pass through fully the cost of higher gas prices, this increase—to take place at the same time as an adjustment in electricity tariffs of 40 percent on average—may compromise the authorities' macroeconomic goals for 2007.

### Key Policy Issues and Discussions

**The main policy issue discussed during the consultation was the need to develop a sustainable and credible external debt management strategy.** The size and rapid disbursement profile of project loans from China over the next three years may put Tajikistan at increased risk of future debt problems, particularly if the authorities' ambitious growth objectives are not achieved. Although concessional in nature, the disbursement of these loans will lead to a rapid reaccumulation of debt, very soon after debt relief was provided under the Multilateral Debt Relief Initiative (MDRI).

**Controlling inflation will require a supportive policy framework.** The authorities' macroeconomic policy framework should continue to be buttressed by a strong fiscal position, and accompanied by a firm commitment to a flexible exchange rate regime, but also reinforced by efforts to strengthen the monetary policy framework. In this connection, the balance sheet of the central bank needs to be put on a stronger footing to give more flexibility and credibility to monetary policy.

**The authorities' medium-term growth objectives are ambitious.** Reaching these goals will require considerable determination on the part of the government to address long-standing problems in the agricultural and energy sectors and to intensify efforts to improve the private investment climate and enhance corporate governance, including for state-owned enterprises. The authorities should also continue with reforms in the fiscal and banking areas.

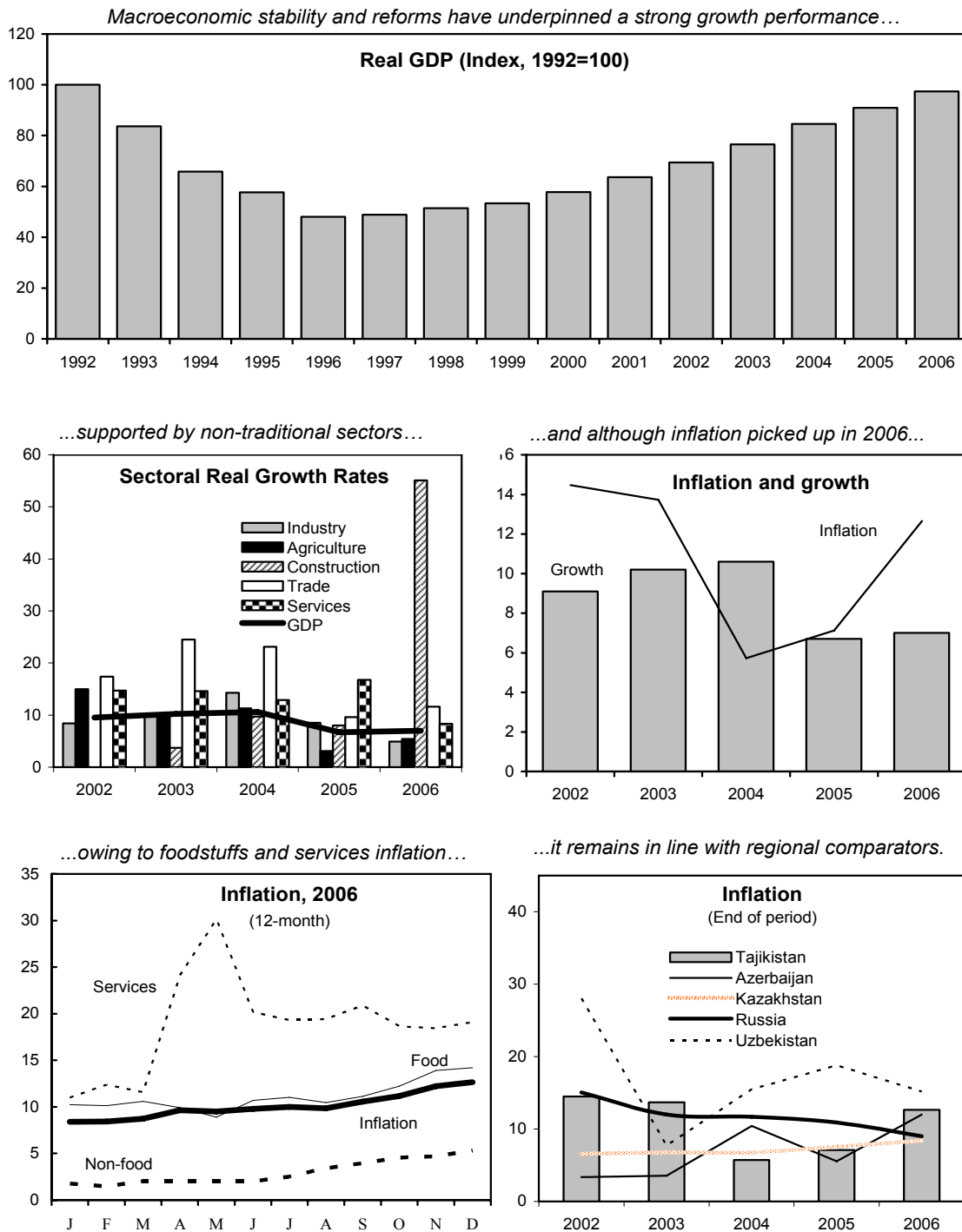
## I. INTRODUCTION AND BACKGROUND

1. **Tajikistan's performance under two ESAF/PRGF arrangements (1998–2005) was strong.** Economic growth during 2002–05 in particular far exceeded program projections, though inflation performance was at times volatile, mostly because of lax monetary policy. A strong fiscal policy stance was the centerpiece of macroeconomic policy efforts (Figures 1–2), with significant remittance flows playing a key role in fostering growth. Moreover, foreign debt has fallen sharply, to a sustainable level. While initial progress in implementing structural reforms in the context of weak institutional capacity was mixed, the authorities' implementation record improved significantly over time, reflecting enhanced program ownership and more streamlined conditionality. Nevertheless, the implementation of some key structural reforms is still pending.
2. **Tajikistan has significant development potential, particularly in the agricultural and electricity sectors.** Much of this potential, however, remains unexploited, primarily because of an uncertain private investment environment and a protracted structural reform process. The authorities' development strategy is currently based on attracting large debt flows in order to benefit from the country's comparative advantage in these sectors, with plans for accompanying sectoral reforms largely at an early stage.
3. **The main policy issue discussed during the consultation was the need to develop a sustainable and credible external debt management strategy.** The size and rapid disbursement profile of project loans from China may put Tajikistan at increased risk of future debt problems (Box 1). Although concessional in nature (with a grant element of 40 percent), the disbursement of these loans will lead to a rapid reaccumulation of debt, very soon after debt relief was provided under the Multilateral Debt Relief Initiative (MDRI).

## II. RECENT POLITICAL AND ECONOMIC DEVELOPMENTS

4. **The political situation remains stable following the November 2006 presidential elections.** President Rakhmonov, who is seen as the sponsor of economic progress and hard-won stability after the civil war, was reelected to a new seven-year term with a significant majority of the votes.
5. **While the recent strong growth performance continued in 2006, inflation accelerated.** Despite considerable disruptions to energy supply late in the year, real GDP growth reached 7 percent, fueled by a surge in construction activity and continuing strong remittance-financed demand for retail services. However, CPI-inflation reached 12.7 percent, its highest level since 2003, mostly as a result of failed harvests and higher gas prices, but also reflecting a relatively passive monetary policy stance and remittance-related demand pressures.
6. **Fiscal policies remained sound despite the election cycle.** The budget recorded a better-than-expected surplus of about 0.8 percent of GDP (excluding the externally-financed Public Investment Program (PIP) and the MDRI grant), reflecting a strong tax revenue performance and the government's decision to refrain from seeking approval for a supplementary budget. Despite the accumulation of tax arrears by the Tajik Aluminum Smelter

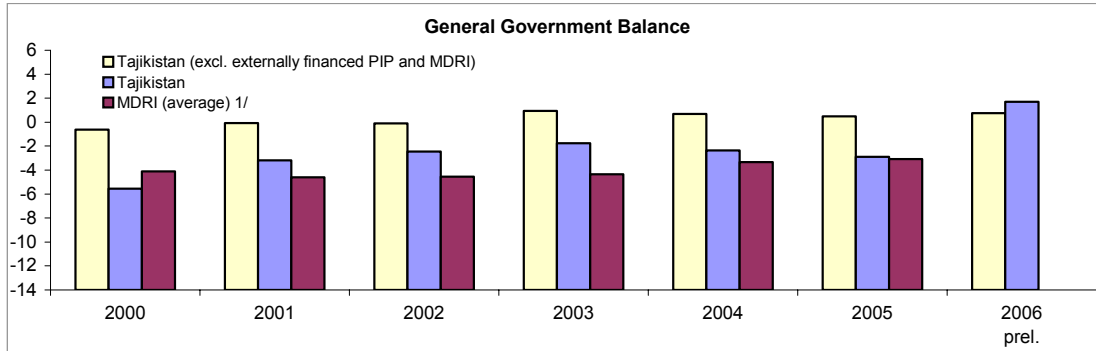
**Figure 1. GDP and Inflation  
(In percent)**



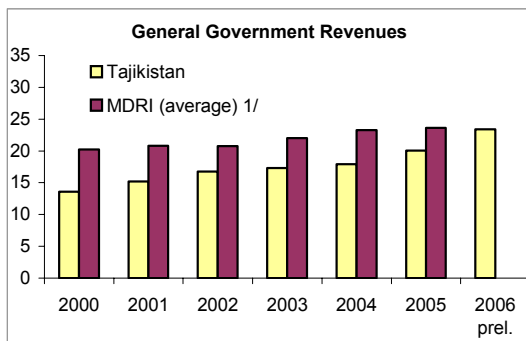
Source: Tajik authorities; WB; WEO; and Fund staff calculations.

**Figure 2. Fiscal Developments  
(In percent of GDP)**

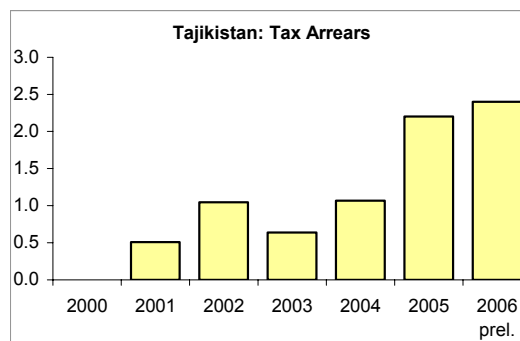
*Fiscal policy continues to be the pillar of macroeconomic stability.*



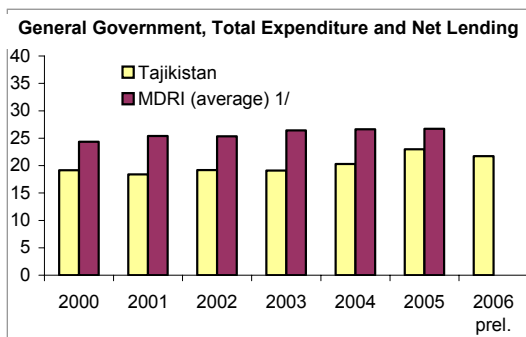
*The strong revenue performance...*



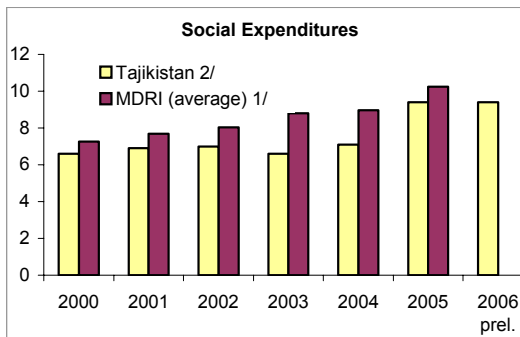
*despite the increase in tax arrears by state enterprises in recent years...*



*helped finance an increase in expenditures...*



*including poverty related spending.*



Sources: Tajikistan authorities, WEO, paper on "HIPC Initiative and MDRI--Status of Implementation", August 2006, and Fund staff estimates.

1/ Excluding Tajikistan.

2/ Data for Tajikistan excludes investment expenditures.



### Box 1. Project Financing from China

**In June 2006, the authorities signed three separate credit agreements totaling about \$604 million with the Export-Import Bank of China.** The loans will be disbursed over the next three years and will finance the construction of two high-voltage electricity lines and the rehabilitation of the road linking Tajikistan and Uzbekistan.

**In January 2007, the authorities signed a memorandum of understanding for an additional \$400 million in financing from China for the construction of new hydropower projects,** thus bringing the total amount of loans to be disbursed by China over the next three years to \$1 billion (about 35 percent of 2006 GDP).

**The World Bank believes that the transmission line and road projects have the potential to contribute to Tajikistan's long-term growth prospects,** if they are implemented according to the original plan and costs, and are accompanied by appropriate sectoral reforms. At this point, however, there is not enough information available to conduct a proper assessment of the economic viability of the new hydropower projects.

Export-Import Bank of China Loan Disbursements 1/ (In millions of U.S. dollars)				
Project Name	Total Cost	Annual Disbursements		
		2007	2008	2009
Total	1003.5	341.4	391.4	270.7
Rehabilitation of Dushanbe-Chanak Highway	281.1	112.4	112.4	56.2
North-South Electricity Transmission Line	267.2	106.9	106.9	53.4
Lolazor-Khatlon electricity Transmission Line	55.2	22.1	22.1	11.0
Hydropower Projects	400.0	100.0	150.0	150.0

Source: Tajik authorities and Fund staff estimates.

1/ The loans, which have a grant element of 40 percent, will have a maturity of 20 years, a 5-year grace period, bear a 2 percent interest rate per annum, and a 0.4 percent banking services fee.

(TadAZ) and the electricity company (Barqi Tajik), tax revenues came in ahead of budgeted levels in part because of higher inflation but also due to strong import growth.<sup>1</sup>

<sup>1</sup> Although tariff-related revenues fell, mostly as a result of the implementation of regional free trade agreements, VAT-related revenues surged as they are not affected by such agreements.

7. **Monetary policy was relatively loose in 2006.** In an effort to keep aggregate demand strong ahead of presidential elections, the central bank refrained from taking an active role in stemming inflationary pressures, and actually reduced its sterilization operations significantly. Moreover, the National Bank of Tajikistan (NBT) provided subsidized loans to the agricultural sector in the last quarter of 2006, partly financed by a \$10 million loan from the Development Bank of China. These developments, however, were partly offset by a significant accumulation of government deposits late in the year. There has been little progress in the deliberations of the commission charged with developing a strategy to securitize the government obligations on the NBT's balance sheet and to recapitalize it. As a result, the NBT relies almost exclusively on reserve requirements and the issuance of its own bills, albeit on a limited basis, to regulate monetary conditions.

8. **The de facto flexibility of the somoni has progressively decreased since late 2004.**<sup>2</sup> The relative stability of the somoni appears to have been supported by the strong growth in workers' remittances rather than by a deliberate attempt to peg the rate, particularly as it has been accompanied by declining NBT intervention in the foreign exchange market (Figure 3). Moreover, the authorities remain committed to a flexible exchange rate regime. There are no signs that the somoni is overvalued, but the export base remains very narrow. Although the current account deficit is projected to widen significantly in the medium term, this reflects the disbursement of significant project financing. Finally, despite significant remittance inflows, the country has not had to deal with the effects of Dutch disease or any significant impact on domestic liquidity yet (Box 2).

9. **Despite record-high aluminum prices, a strong performance in noncotton agricultural exports, and the continued rapid growth of workers' remittances, external accounts did not improve commensurately.** Since Tajikistan does not mine the raw material for aluminum production, but rather relies on an export processing agreement with its foreign suppliers for its processing, export performance did not fully benefit from higher aluminum prices in 2006.<sup>3</sup> While workers' remittances continued to grow at a very rapid pace, these flows were just enough to offset the increase in the trade deficit resulting from higher energy import prices and buoyant demand for imported consumer and foreign-financed capital goods. Gross reserves remain relatively low, at the equivalent of about two months of imports.

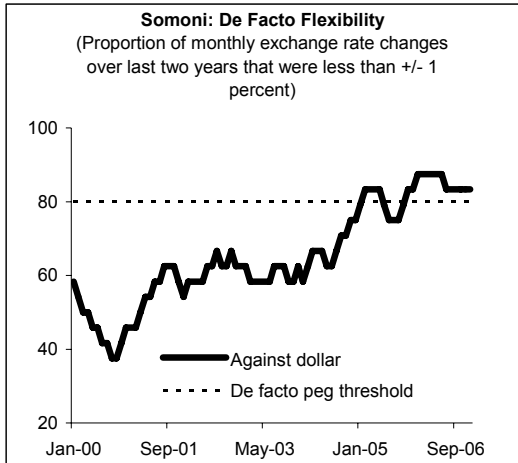
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<sup>2</sup> According to a classification developed in Reinhart and Rogoff (2004), an exchange regime could be classified as a de facto peg when the proportion of monthly exchange rate changes over the previous two years falling within a +/- 1 percent range exceeds 80 percent.

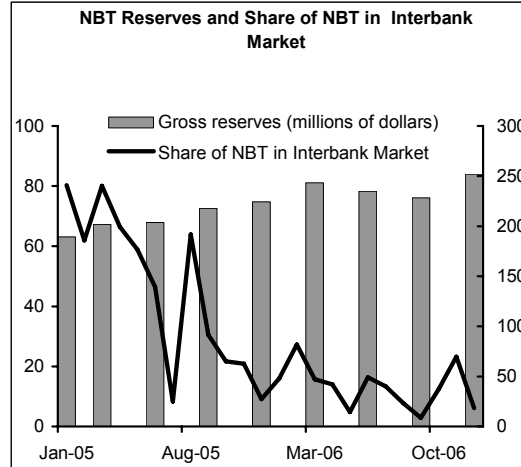
<sup>3</sup> According to the authorities, TadAZ receives a fixed pre-negotiated fee for the processing of alumina. This arrangement has been in effect since 2005, and in 2006 the fee was \$410 per ton of aluminum. The details of the arrangement are not fully transparent.

**Figure 3. Exchange Rate Developments**

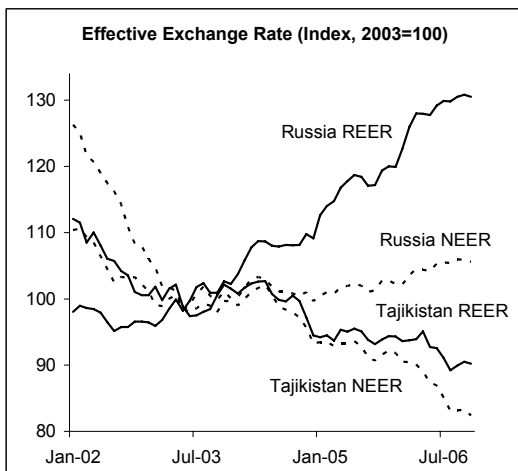
*The volatility of the exchange rate decreased...*



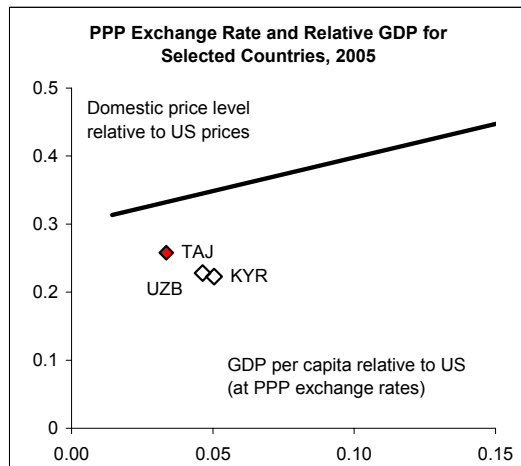
*...with limited intervention...*



*...while competitiveness has improved...*



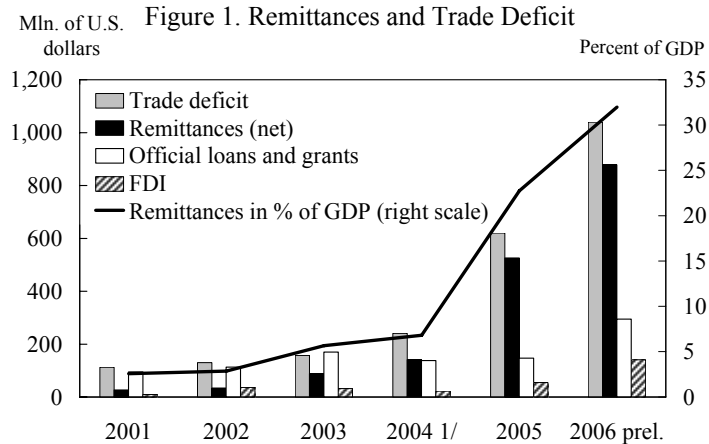
*...with the exchange rate still below its equilibrium PPP level.*



Source: Tajik authorities; IFS; and Fund staff calculations. See Reinhart and Rogoff (2004) for details on their methodology for measuring de facto flexibility.

### Box 2. The Role of Remittances in Tajikistan

In recent years, remittances have grown exponentially, and have emerged as the main source of financing of the trade deficit, **outstripping official loans and grants** (Figure 1). Although the increase can be partially explained by improvements in the quality and coverage of data, the magnitude of these flows is evident. Unsatisfactory job prospects in Tajikistan and buoyant recent growth in Russia—the origin of about 90 percent of remittances—where monthly dollar wages have tripled since 2001, contributed to this growth.

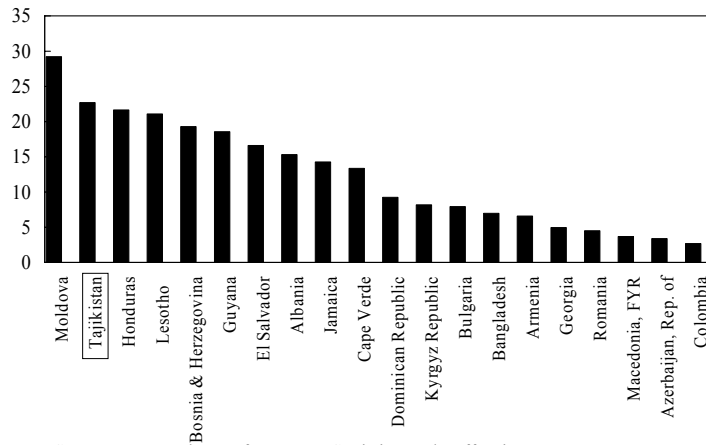


Sources: National authorities; and staff estimates.  
1/ Data net of 250 mln. of debt-equity swap with Russia.

Recorded remittances to Tajikistan are among the highest in the world as a percentage of GDP (Figure 2).

By supporting consumption and expenditure on health and education, remittances have contributed to growth and poverty reduction. So far, there has been no evidence of appreciation pressure via either a rapid accumulation of reserves or nominal appreciation. Three factors likely explain this (1) high import content of remittances inflows; (2) accumulation of remittances proceeds in the form of cash, rather than bank deposits; and (3) high dollarization of the Tajik economy.

Figure 2. Remittances in Percent of GDP, 2005



Sources: IMF, Balance of Payments Statistics; and staff estimates.

**A strong macroeconomic policy framework and continued progress with financial stabilization and structural reforms are needed to respond to challenges that remittances may pose.** Reliance on remittances to finance consumption and investment may make the economy more vulnerable to external economic and political developments. A well-targeted social safety net is needed to protect the poorest in the case of interruption of remittances.

### III. POLICY DISCUSSIONS

10. The Article IV discussions focused on a) the debt sustainability implications of the authorities' debt-based development strategy; and b) policy challenges to keep inflation under control while sustaining growth. The mission also discussed prospects for reinvigorating structural reform efforts and possible support under the Policy Support Instrument (PSI).

#### The Debt Issue

11. **The authorities explained that their development strategy involved a very rapid accumulation of external debt, on concessional terms, over the next three years.** After lowering the external debt-to-GDP ratio to an estimated 31 percent by end-2006—mostly as a result of a debt restructuring operation with Russia and MDRI relief—the authorities' plans to go ahead with the contracting of \$1 billion of concessional loans from China would bring that ratio to a projected 56 percent by end-2009. In NPV terms, the debt-to-GDP ratio would rise to about 45 percent (from 25 percent now), compared with a DSA threshold of 30 percent, and would remain above this threshold for a number of years. The DSA prepared by staff, jointly with the World Bank, shows that debt dynamics would seriously deteriorate should economic growth not materialize at the rates forecast by the authorities (Appendix I).<sup>4</sup>

12. **While mindful of the implications for debt sustainability of contracting these loans,** the authorities argued that their current debt management strategy is geared towards the promotion of regional economic integration, enhancing growth prospects in the longer term and reducing poverty. Specifically, they noted that they are looking to finance projects that would alleviate existing domestic and regional transportation bottlenecks, allow for increased trade in the region (most importantly in electricity and agricultural products), and improve domestic infrastructure. They also stressed that the Chinese government was the only available source of concessional financing for these critical projects. They nonetheless agreed with staff that proper project vetting mechanisms needed to be put in place at the earliest, possibly with external assistance.

13. **The authorities stated that they intended to be constrained by a medium-term foreign debt ceiling of 60 percent of GDP.** Staff indicated that the planned pace of debt accumulation, even if constrained by this ceiling, would greatly increase the risk of future debt problems for Tajikistan, particularly as plans for supporting sectoral reforms remain largely unclear. Specifically, the lack of a well-defined electricity regulatory regime, problems with payment discipline on the part of state-owned enterprises, and remaining distortions in the agricultural sector, which could benefit the most from the road project, create uncertainty about the economic viability of the projects in question. Moreover, staff expressed concerns that the rapid accumulation of debt would put additional pressure on the budget, as significant counterpart funds would be needed, which would reduce resources available for other key priority sectors and affect macroeconomic performance.

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<sup>4</sup> Tajikistan is now classified as a “medium performer” by the World Bank, which would imply a threshold of 40 percent. However, recent guidance from the Executive Board requires the use of three-year CPIA average scores in cases of rapid debt accumulation.

## Challenges to Controlling Inflation While Sustaining Growth

14. **Inflation risks for 2007 are on the upside, mostly because of the recent decision by Uzbekistan to double gas export prices.**<sup>5</sup> While staff welcomed the authorities' decision to pass through fully the cost of higher gas prices, this increase—to take place at the same time as an adjustment in electricity tariffs of 40 percent on average—may compromise the authorities' original goal of 7½ percent growth and 7 percent inflation for 2007. Since the inflation target was likely to prove especially challenging, the authorities considered that it would be more credible to aim for inflation in the range of 8–9 percent, particularly when taking into account the worse-than-expected 2006 outcome. While a strong fiscal stance would remain central in the fight against inflation, the NBT agreed with staff that they should also remain vigilant and tighten monetary policy as required to avoid second-round price effects from higher energy prices, and that a flexible exchange rate framework should be maintained.

15. **Based on approved expenditure plans, a continuation of the strong 2006 tax revenue performance would likely lead to a small fiscal surplus in 2007.** The authorities argued, however, that they wanted to stick to their original budget deficit target of 1 percent of GDP, to allow for higher social expenditures and support wage reform, which would require the approval of a supplementary budget later in the year. Staff noted that under current expenditure plans, a significant increase in these areas is already contemplated, including a larger allocation for the energy compensation mechanism and higher wages and pensions (½ percent of GDP in total), financed in part by MDRI resources. As such, staff urged the authorities to save a large part of any revenue overperformance, particularly at a time when inflation was on an upward trend and debt dynamics were worsening, and that, at a minimum, a supplementary budget should not be considered until the inflation picture had sufficiently improved.

16. **The NBT noted that, because of a lack of progress in resolving the large outstanding debt of the cotton sector and the absence of appropriate financing mechanisms,** there were strong pressures to provide financial resources to the agricultural sector, which could undermine inflation performance. The authorities stressed that they were working with the Asian Development Bank (ADB) and the World Bank as lead agencies in resolving the debt of the cotton sector—incurred by farms under a complex system of in-kind credit from intermediaries—and in designing a mechanism for financing the agricultural sector, which would be accompanied by appropriate sectoral reforms. The mission encouraged the authorities to continue to work closely with the lead agencies to find a solution to this critical problem, while noting that the FSAP team could provide assistance in evaluating the merits of any draft resolution plan.

17. **There has been little progress in strengthening the balance sheet of the NBT.** The authorities stressed that, while they remain committed to enhancing the marketability of the stock of government securities held by the NBT and restoring the capital position of the NBT, moving forward with specific steps, especially on recapitalization, required a careful

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<sup>5</sup> Uzbekistan, which has a monopoly in the supply of gas to Tajikistan, raised gas exports prices to Tajikistan from \$55 to \$100 per thousand cubic feet as of January 1, 2007.

assessment of the accounting and legal implications of carrying out such efforts. The mission urged the authorities to implement without further delay the recommendations of the March 2006 MCM technical assistance mission in the area of monetary operations, and to continue to seek support from the MCM regional advisor on these matters. Moreover, given the complexity of the subject, the mission encouraged the authorities to seek technical assistance from MCM in the area of central bank recapitalization.

### **Reinvigorating Structural Reforms**

18. **The medium-term prospects are good, but not without risks**, particularly as the role of remittances in sustaining high rates of growth and reducing poverty could be expected to diminish, and may be affected by potential restrictions in the movement of workers. In the medium term, the authorities intend to reduce inflation to an average of 6 percent, while GDP growth is projected at an average rate of 8 percent a year. Further new investment in infrastructure and the energy sector, coupled with the commissioning of the Sangtuda I hydroelectric project, will continue to boost construction and the services sector. The agricultural sector is also expected to benefit from continued strong demand from Russia and Kazakhstan. The authorities nevertheless agreed that reaching these goals requires a reinvigoration of their efforts to stimulate private investment and diversify Tajikistan's export and production base. Specifically, the authorities recognize that there is an urgent need to address long-standing policy issues in the agricultural and energy sectors.

19. **The authorities reaffirmed their commitment to pushing ahead with the outstanding structural reform agenda**, but recognized that some difficult steps are still to be taken:

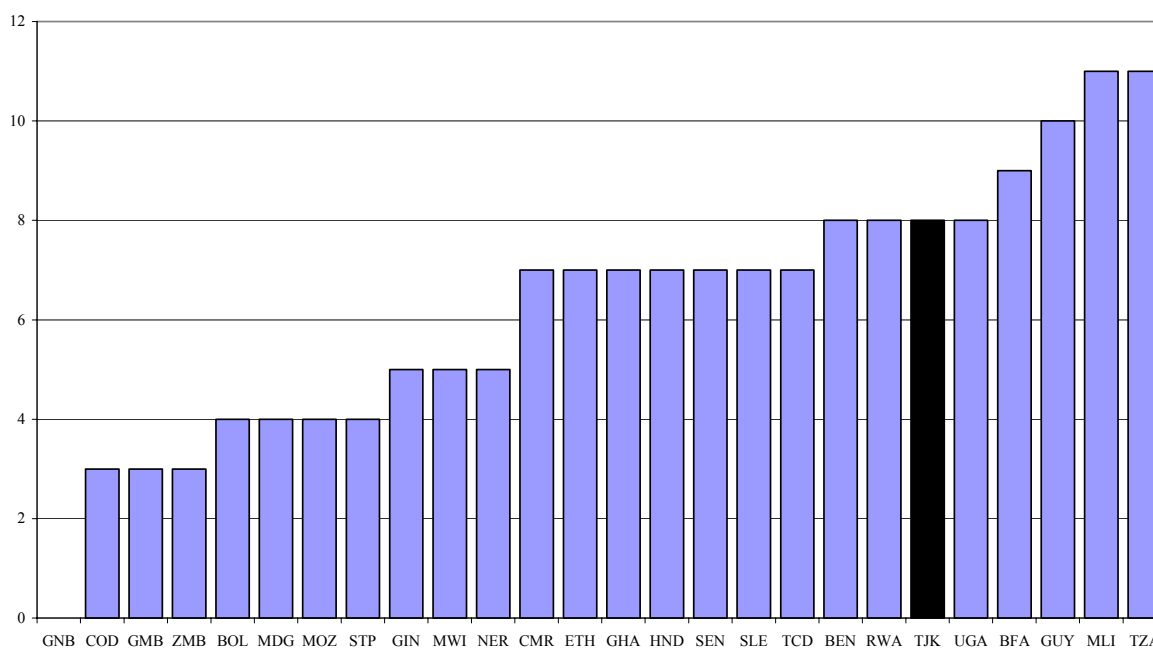
- On **fiscal structural reforms**, significant progress has been achieved in the areas of tax administration and public financial management (Boxes 3–4). Nevertheless, the authorities need to urgently address remaining weaknesses in tax compliance and financial monitoring of state enterprises.
- **The banking sector is now stronger but remains small and vulnerable** (Figure 4). The banking system appears well-capitalized and profitable, but despite rapid growth in credits and deposits in recent years, it remains small and is heavily dollarized. Although nonperforming loans have declined, they are still relatively high by international standards and provisioning may be insufficient. Moreover, public disclosure requirements are inadequate and, despite legal amendments introduced late in 2005, foreign competition is still very limited. An FSAP assessment is currently underway and is expected to inform the authorities' reform agenda.
- While there has been some progress in improving **the finances of the energy sector**, a large agenda remains. Notably, structural and regulatory weaknesses in the electricity sector continue to undermine its enormous potential. While a first adjustment of 25 percent was enacted on February 1, 2007, further significant increases in electricity tariffs are needed to make the electricity sector financially viable. Moreover, a formal regulatory framework for the electricity sector is still missing, which may explain the lack of more interest from potential foreign investors.

### Box 3. Tajikistan: Improvements in Public Financial Management System

In recent years, Tajikistan achieved important progress in improving fiscal transparency and strengthening key public financial management (PFM) areas. The recent Fiscal ROSC and FAD technical assistance missions concluded that (a) the roles and responsibilities of the executive, legislature, and judiciary are clearly defined; (b) reporting on the budget to parliament and the general public has strengthened in recent years; (c) the stock of expenditure arrears has been dramatically reduced and there is no accumulation of new arrears; (d) the creation of a budget institution has strengthened public financial accountability; and (e) the law on State Finance has markedly strengthened the regulatory framework of the budget process.

This improvement was also acknowledged in the staff assessment of Tajikistan's qualification for the MDRI (Republic of Tajikistan—Staff Assessment of Qualification for the Multilateral Debt Relief Initiative, December 8, 2005 ([www.imf.org](http://www.imf.org))). The assessment concluded that the country's core PFM system works reasonably well and compares favorably to that of a number of other HIPCs that qualify for debt relief.

Tajikistan and HIPC Countries: Number of Assessment and Action Plan (AAP) Measures Fully Implemented



Source: IMF-World Bank paper "Update on the Assessments and Implementation of Action Plans to Strengthen Capacity of HIPCs to Track Poverty-Reduction Public Spending", April 2005 (Country Report No. 05/177) and Tajikistan's "Staff Assessment of Qualification for the MDRI" December 2005 .

#### Despite progress so far, Tajikistan still faces some key challenges in improving its public finance systems.

The monitoring of financial operations of state-owned enterprises deserves greater attention and scrutiny to identify and report on contingent liabilities and quasi-fiscal activities of these enterprises. Likewise, the design and implementation of a new commitment control system in harmony with the implementation of the new decentralized procurement system should be in place to avoid recurrence of expenditure arrears. While Tajikistan's budget process has improved, the authorities need to develop an organizational classification in line with international standards for budget preparation and execution, clearly demarcate the boundaries between the general government sector and the broader public sector, and strengthen the link between policy and budgeting.



#### Box 4. Tajikistan: Reforms in Revenue Administration

**An important element of the reform program of the government has been the modernization of the revenue administration framework, where early reform efforts have contributed to the strong growth in tax revenues.** These achievements have laid the foundation for further reforms needed to lift Tajikistan's level of collections which, despite steady improvement during the past five years, still remains at the lower end of the scale among CIS countries.

CIS: Tax Revenue, 2000-05  
(In percent of GDP)

	2000	2001	2002	2003	2004	2005
Armenia	14.8	14.3	14.6	14.0	14.0	14.3
Azerbaijan 1/	14.5	14.6	15.1	15.4	15.4	16.0
<b>Tajikistan</b>	<b>12.9</b>	<b>14.1</b>	<b>15.0</b>	<b>15.0</b>	<b>15.2</b>	<b>16.6</b>
Georgia	11.8	12.0	14.4	14.5	18.4	19.8
Kyrgyz Republic	15.1	15.7	17.5	17.7	18.3	20.2
Uzbekistan	26.2	23.4	22.9	22.7	22.6	21.5
Kazakhstan	20.2	22.3	21.0	23.2	22.3	26.3
Moldova	25.0	24.4	25.8	27.5	29.8	31.1
Ukraine	28.1	27.9	30.3	30.6	29.2	35.4
Belarus	33.6	32.5	37.2	38.0	38.2	39.6
Russia	35.1	35.0	35.1	34.1	35.6	41.8

Sources: Staff reports and MCD database.  
1/ Central government

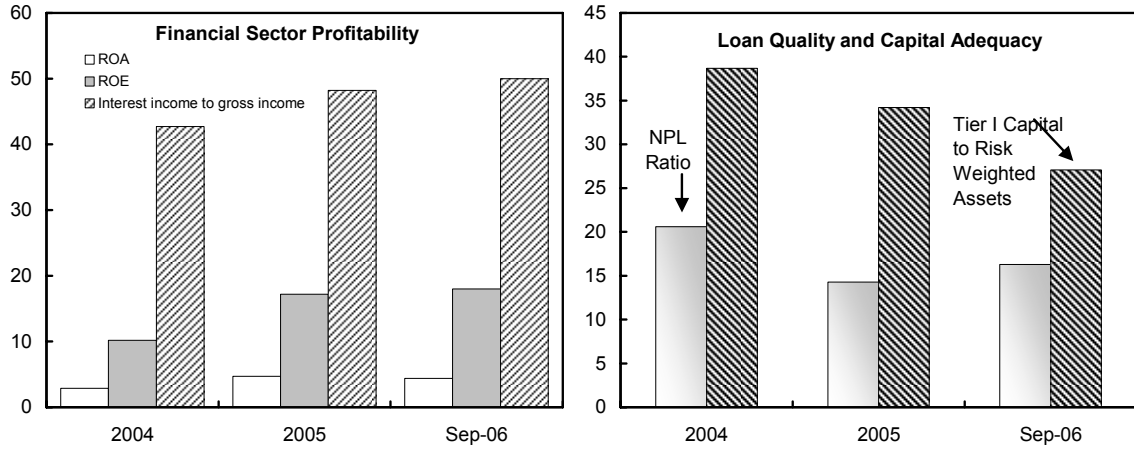
**With technical assistance from donors, including the IMF, the authorities have made significant progress over the past 3–4 years** in the areas of legislation (new tax and customs codes were introduced in 2005), restructuring the tax department along functional lines, clarifying the responsibility of tax administration for the collection of social security taxes, and introducing new procedures and systems.

**Nevertheless, the full implementation of several key reforms is lagging, partly due to personnel capacity constraints.** Almost two years after the adoption of new tax and customs codes, the authorities have been able to adopt only half of the required supporting regulations. Tax arrears have increased substantially in recent years, particularly those of state-owned enterprises. The ongoing restructuring of the tax department along functional lines also needs to be completed.

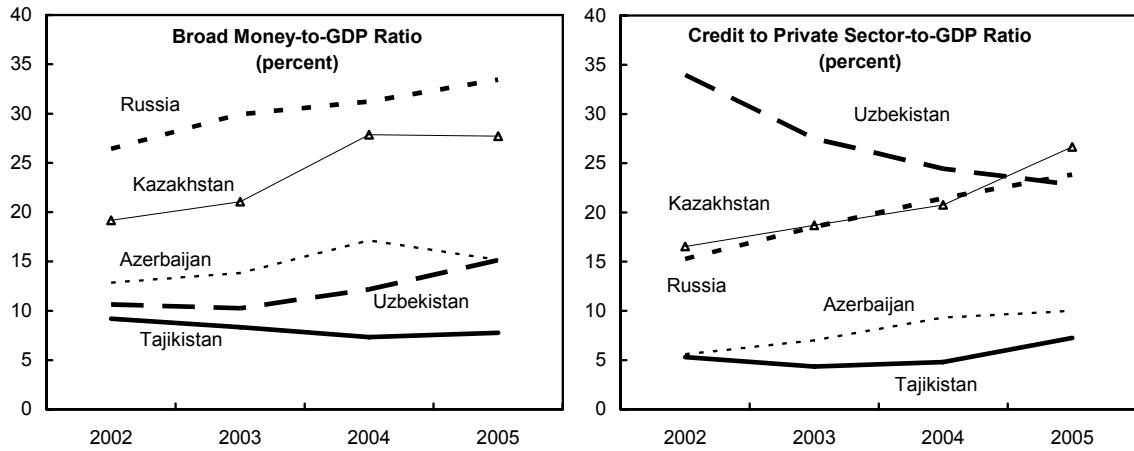
- While the government has made some headway on **land reform**, distortions remain. Even though a significant number of land share certificates were issued to private farmers, restructured farms are still subject to implicit state control over production and harvesting decisions, particularly in the cotton sector. Finally, there is an urgent need to facilitate the use of share certificates as collateral for obtaining bank financing.

### Figure 4. Financial Sector Progress and Challenges

*The banking sector is stronger, but much remains to be done...*

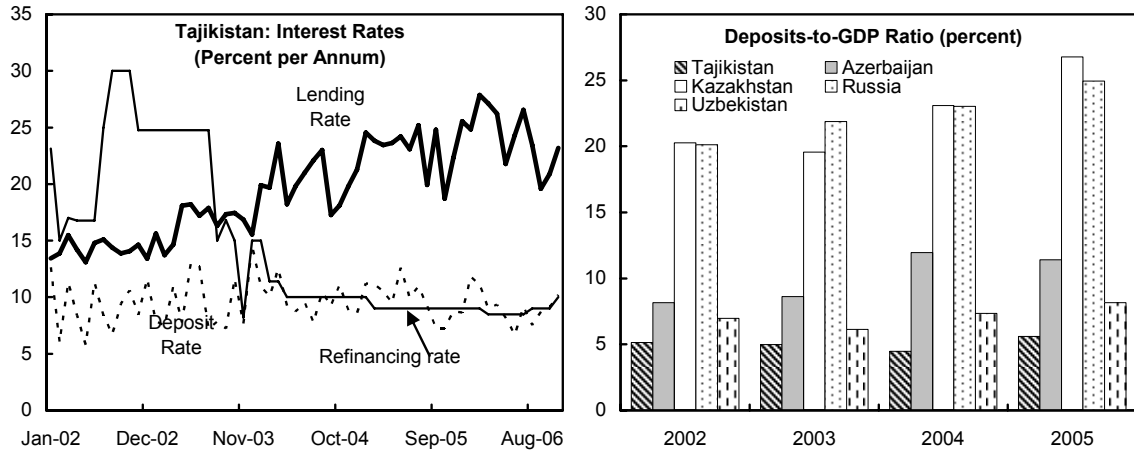


*... as intermediation and private sector credit remains low, even by regional standards...*



*... spreads are high...*

*... and confidence in the system still lacking.*



Source: Tajik authorities; WEO; IFS; and Fund staff calculations.

- President Rakhmonov told the mission that **governance** concerns, which continue to plague Tajikistan, are seriously affecting the business climate and private sector growth (Box 5). Staff welcomed the legislative changes that were introduced in 2006 to cut down on bureaucratic and overly complex regulatory and licensing procedures. Nevertheless, the implementation of the approved procedures has been slow and accompanying regulations have not been approved. Efforts to privatize large state-owned enterprises and improve corporate governance are lagging.

### **A Possible PSI-supported program**

20. **The authorities explored with the mission a possible PSI.** They felt that Fund support, in the form of a PSI, could be important for safeguarding the macroeconomic stability achieved under the previous PRGF arrangement, accelerating structural reform, and enhancing the role of the private sector in fostering economic growth. They also expressed their commitment to continue with the reforms of core institutions, specifically in the areas of revenue administration, public expenditure, and the design and implementation of monetary policy. However, the authorities and the staff were unable to reach understandings on the appropriate borrowing policies (see paragraphs 11–13).

### **Other Issues**

21. The authorities are in the process of completing their second **Poverty Reduction Strategy Paper (PRSP2)** to cover the period of 2007–09. They expect to complete the PRSP2 in the first quarter of 2007, before holding a donors’ meeting, which they have asked the World Bank to organize to seek pledges for its implementation. The PRSP2 is expected to focus on efforts to improve the private investment climate and the consolidation of their public sector reform program.

22. **Tajikistan continues to pursue membership of the WTO**, which the authorities believe would provide a boost to exports, investment and growth in Tajikistan. While Tajikistan has a relatively low-tariff open trade regime, the WTO Accession Working Party has noted that issues remain relating to market access in services, electricity subsidies, as well as discriminatory rules toward foreign investors’ participation in the privatization process. Despite some progress in improving bilateral relations, bottlenecks remain in trade and transit relations with Uzbekistan. In that regard, the accession of Uzbekistan to the Eurasian Economic Community (EAEC) is expected to serve as a catalyst for progress in this area.

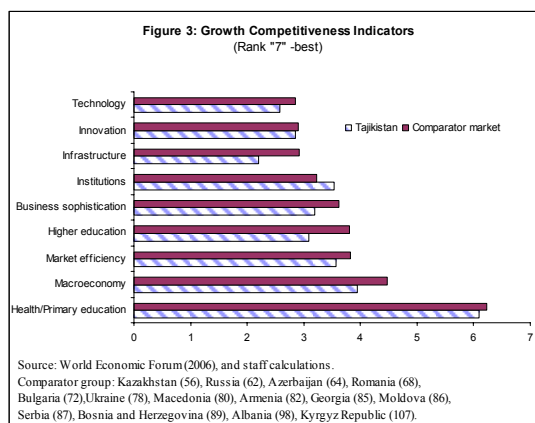
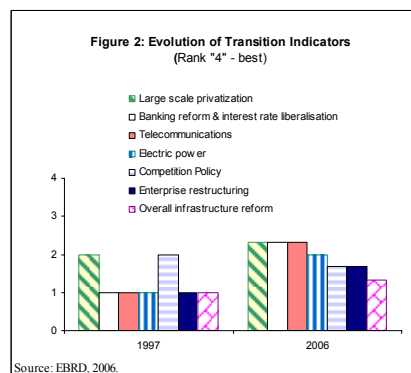
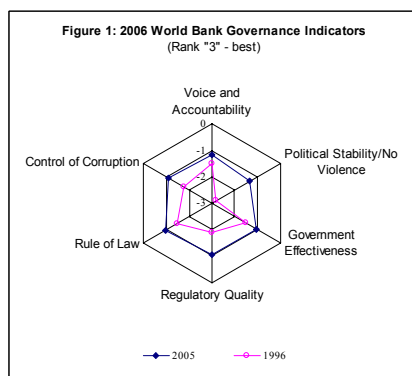
23. A LEG technical assistance mission in late 2006 found that the second draft of a new **AML/CFT** law addresses some of the shortcomings identified in an earlier version of the draft law. Nevertheless, the mission also found that the law still falls short of international standards and further work is needed, including a formal decision on the responsibilities and governance structure of the proposed Financial Intelligence Unit, and thus is unlikely to be adopted before the second half of 2007.

### Box 5: Private Investment Climate

The **World Bank's Governance Indicators** rank Tajikistan rather low on all five key indicators (Figure 1). Transparency International also assigns the country a low score of 2.2 and a rank of 142 out of 158 countries on its **Corruption Perception Index (CPI)**, and a regional rank of 17 out of 21 countries sampled. While rankings indicate slow progress in this area, improving governance has recently been placed high on the list of government priorities.

The **World Bank's Doing Business in 2006** ranks Tajikistan at 133 out of 175 countries. Its best ranking is achieved in such categories as employment laws, registering property, enforcing contracts, and closing a business (all above rank 50), while poor ranking is observed in protecting investors (rank 174), starting a business (rank 166), trading across borders (rank 163), paying taxes (rank 154), and getting credit (rank 143). The trading across borders category stands out especially: it takes an average of 12 documents, 58 days and \$3,925 to carry out foreign trade transactions, compared to the regional average of 9 documents, 33 days and \$1,519.

According to the **EBRD's Transition Indicators**, Tajikistan has lagged behind most transition economies in the region (Figure 2). The **World Economic Forum's Growth Competitiveness Index (GCI)** places Tajikistan 96 out of 125 assessed countries. However, its performance does not diverge significantly from its comparators (Figure 3).



## IV. STAFF APPRAISAL

24. **The authorities' debt-based development strategy entails substantial risks to debt sustainability in the longer term.** In the absence of appropriate project vetting mechanisms, and delays in implementing key sectoral reforms, the prospective significant debt accumulation

in the coming years could lead to debt-servicing problems in the future, particularly if the authorities' ambitious growth objectives are not achieved. Staff therefore urges the authorities to put in place a well-defined debt management strategy that would include cautious limits on the accumulation of new debt, reaffirm their commitment to contract debt only on a concessional basis, and set up appropriate vetting mechanisms to assess the economic viability of proposed projects.

25. **The authorities expressed interest in a PSI-supported program.** Staff recognizes that a Fund arrangement could be beneficial for a country that, despite recent gains, remains among the poorest in the region. However, while the authorities have broadly followed Fund advice and appear more committed to reform than in the early years of engagement, they are determined to pursue their debt-based development strategy. In view of the substantial risks this entails to debt sustainability, staff does not consider the strategy to be appropriate.

26. **Controlling inflation will require a supportive policy framework.** Staff believes that the authorities' macroeconomic policy framework should continue to be buttressed by a strong fiscal position, and accompanied by a firm commitment to a flexible exchange rate regime, but also reinforced by efforts to strengthen the monetary policy framework. The authorities should save a large part of any revenue overperformance in 2007. Moreover, the balance sheet of the central bank needs to be put on a stronger footing to give more flexibility and credibility to monetary policy. Given the balance sheet problems of the central bank, the policy of directed credits should be ended. Any financial resources, particularly if subsidized, should be channeled through the budget in a transparent manner.

27. **Staff welcomes the central bank's continued commitment to a managed exchange rate float,** with intervention in the foreign exchange market limited to smoothing operations and shoring up the reserve coverage.

28. **The authorities' medium-term growth objectives are ambitious, but achievable.** Reaching these goals will require considerable determination on the part of the government to address long-standing policy issues in the agricultural and energy sectors and to intensify efforts to improve the private investment climate and enhance corporate governance, including for state-owned enterprises. In this regard, while initial steps to adjust electricity prices are welcome, a properly defined regulatory framework needs to be put in place as soon as possible to allow the country to take full advantage of its potential in this sector. Similarly, staff encourages the authorities to ensure that production decisions in the agricultural sector are not subject to political interference and to continue to work closely with the ADB and the World Bank in finding an equitable and macroeconomically sound solution to the cotton debt problem. The authorities should also continue with ongoing reforms in the fiscal and banking sector areas.

29. It is proposed that the next Article IV consultation with Tajikistan takes place on the standard 12-month cycle.

Table 1. Tajikistan: Selected Macroeconomic Indicators, 2003–07

(Quota: SDR 87 million)

(Population: 6.5 million)

(Per capita GDP: \$357, 2005)

	2003	2004	2005	2006 Prel.	2007 Staff Proj.
(Annual percent change, unless otherwise indicated)					
National accounts					
Nominal GDP (in millions of somoni)	4,758	6,158	7,201	9,272	10,867
Nominal GDP (in millions of dollars)	1,555	2,073	2,311	2,811	3,141
Real GDP	10.2	10.6	6.7	7.0	7.5
CPI inflation (end-of-period)	13.7	5.7	7.1	12.7	9.0
Unemployment rate	2.4	2.3	2.3	2.3	...
Poverty rate (in percent of population)	63.0	57.0	...	...	...
(In percent of GDP)					
Investment and savings 1/					
Investment	13.1	14.9	14.8	13.5	26.7
Fixed capital investment	12.0	13.5	13.8	12.6	25.8
Government	6.5	8.1	7.8	6.6	18.8
Private	5.5	5.4	6.0	6.0	7.0
Gross national savings	11.9	10.9	12.3	11.1	11.6
Public	4.8	5.8	4.9	4.9	4.7
Private	7.1	5.1	7.4	6.2	6.8
Savings/investment balance	-1.3	-3.9	-2.5	-2.5	-15.2
(In percent of annual GDP)					
Revenue and grants 2/	17.3	17.9	20.1	23.4	20.7
Of which: tax revenue	15.0	15.2	16.6	16.5	16.5
Expenditure and net lending	19.1	20.3	23.0	21.7	34.8
Of which: current	12.6	12.1	15.1	15.0	15.9
capital	6.5	8.1	7.8	6.6	18.8
Balance (excluding externally-financed PIP and MDRI)	0.9	0.7	0.5	0.8	0.4
Balance (including externally-financed PIP and MDRI) 2/	-1.8	-2.4	-2.9	1.7	-14.1
Domestic financing	-1.1	-1.7	0.3	-3.3	0.5
External financing	2.8	4.0	2.6	1.6	13.6
(12-month growth in percent of broad money, unless otherwise indicated)					
Net foreign assets of the banking sector	47.7	-21.9	5.4	74.9	-0.9
Net domestic assets of the banking sector	-20.9	77.4	14.0	-47.6	21.2
Broad money	28.6	14.1	23.9	40.6	20.4
Bills payable	-1.8	41.4	-4.5	-13.3	0.0
Velocity of broad money (four-quarter average)	3.0	3.7	3.5	3.3	3.1
Interest rate (28-day NBT bill rate, in percent)	4.9	6.2	7.0	10.7	...
(In millions of U.S. dollars, unless otherwise indicated)					
External sector 3/					
Exports of goods and services	985	1,211	601	668	734
Percent change	23.2	22.9	...	11.0	9.9
Imports of goods and services	1,142	1,451	1,221	1,646	2,329
Percent change	22.9	27.1	...	34.8	41.5
Current account balance	-20	-82	-58	-70	-476
Percent of GDP	-1.3	-3.9	-2.5	-2.5	-15.2
Total public and publicly guaranteed external debt	990	824	887	859	1,265
Percent of GDP	63.7	39.7	38.4	30.6	40.3
Gross official reserves	135	189	224	252	284
Months of imports	1.8	2.5	2.1	1.7	1.8
Months of imports (excl. bartered electricity and imports financed by loans from China)	...	...	2.1	2.0	2.1
Memorandum items:					
Nominal effective exchange rate (Index 2000=100)	63.3	62.6	58.6	...	...
Real effective exchange rate (Index 2000=100)	93.0	93.1	87.8	...	...
Average exchange rate (somon per dollar)	3.06	2.97	3.12	3.3	...

Sources: Data provided by the Tajikistan authorities; and Fund staff estimates.

1/ Private investment and savings are estimates.

2/ Fiscal revenues and balance include the MDRI grant in 2006, and the PIP expenditure include investment financed by loans from China.

3/ Projections for 2006 and 2007 are based on projections of the disbursement profile of loans from China. Starting from 2005,

the export and import figures reflect the transition to tolling arrangement for aluminum exports. Therefore, the export and import figures are lower than earlier years.

Table 2. Tajikistan: Basic Social Indicators, 1970–04

	Tajikistan				Europe and Central Asia 1/	Low- income countries 1/
	1970–75 2/	1980–85 2/	1990–99 2/	2000–04 1/		
<b>Population</b>						
Life expectancy at birth (in years)	60	63	63	64	69	59
Infant mortality (per thousand live births)	...	94	90	75	28	79
Birth rate, crude (per thousand people)	40	39	36	29	13	29
Death rate, crude (per thousand people)	10	8	8	7	12	11
Fertility rate (in births per woman)	7	6	5	4	2	4
Age dependency ratio (in percent)	1	1	1	1	0	1
Rural population (in percent of population)	64	66	71	75	36	69
Urban population (in percent of population)	36	34	29	25	64	31
<b>Health indicators</b>						
Child immunization: Measles (in percent of children under 12 months)	...	...	85	89	93	64
Child immunization: DPT (in percent of children under 12 months)	...	...	81	82	93	67
Physicians (per thousand people)	...	3	2	2	3	0
Hospital beds (per thousand people)	...	11	9	6	8	1
<b>Education</b>						
Gross primary school enrollment rate (in percent of age group)	...	...	94	100	102	100
Gross secondary school enrollment rate (in percent of age group)	...	...	88	81	92	46

Sources: World Development Indicators; the World Bank Group.

1/ Latest data available.

2/ For some years there is no available data.

Table 3. Tajikistan: General Government Operations, 2005-07  
(In percent of GDP; unless otherwise indicated)

	2005	2006	2007				
	Act.	Prel.	Q1	Q2	Q3	Q4	Year
			Staff Proj.				
Overall revenues and grants	20.1	23.4	4.4	4.8	4.9	6.5	20.7
Total revenues	19.3	18.7	4.1	4.5	4.6	5.5	18.7
Tax revenues	16.6	16.5	3.7	4.1	4.2	4.5	16.5
Income and profit tax	2.1	2.1	0.5	0.6	0.5	0.6	2.2
Payroll taxes	2.1	2.0	0.4	0.5	0.5	0.6	2.0
Property taxes	0.8	0.8	0.1	0.2	0.2	0.3	0.8
Internal taxes on goods and services	9.4	9.7	2.2	2.4	2.5	2.6	9.8
VAT	6.8	7.3	1.6	1.8	1.9	2.0	7.3
Excises and other internal indirect taxes	2.5	2.5	0.6	0.6	0.6	0.7	2.5
International trade and operations tax	2.1	1.8	0.4	0.4	0.4	0.5	1.6
Other taxes	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Non-tax revenues 1/							
Grants 2/	0.7	4.7	0.3	0.3	0.3	1.0	1.9
Of which: PIP financing	0.0	0.6	0.3	0.3	0.3	0.3	1.3
Total expenditures and lending minus repayments 3/	23.0	21.7	7.6	8.5	8.8	9.8	34.8
Current expenditures	15.1	15.0	3.2	3.9	4.0	4.9	15.9
Expenditures on goods and services	10.4	10.4	2.1	2.7	2.8	3.4	11.0
Wages and salaries	3.7	4.1	0.9	1.1	1.0	1.4	4.4
Others	6.7	6.3	1.1	1.6	1.8	2.0	6.6
Interest payments	0.5	0.5	0.1	0.1	0.2	0.2	0.6
Transfers and subsidies	4.2	4.1	1.0	1.0	1.0	1.2	4.3
Of which: Compensation scheme for energy tariff increases	0.0	0.2	0.1	0.1	0.1	0.1	0.2
Capital expenditures	7.8	6.6	4.4	4.6	4.8	4.9	18.8
Externally financed PIP	3.4	3.1	3.9	3.9	3.9	3.9	15.7
Of which: loans from China	0.0	0.0	2.7	2.7	2.7	2.7	10.9
Domestically financed 1/	4.4	3.5	0.5	0.7	0.9	1.0	3.1
Lending minus repayments	0.1	0.1	0.0	0.0	0.0	0.0	0.0
Overall balance (incl. externally financed PIP and MDRI)	-2.9	1.7	-3.2	-3.7	-3.9	-3.4	-14.1
Overall balance (excl. ext. financed PIP, PIP related grants and MDRI) 4/	0.5	0.8	0.4	-0.1	-0.3	0.3	0.4
Total financing (incl. externally financed PIP and MDRI)	2.9	-1.7	3.2	3.7	3.9	3.4	14.1
Net external	2.6	1.6	3.4	3.4	3.4	3.4	13.6
Disbursements	3.6	2.9	3.6	3.6	3.6	3.6	14.5
Program loans	0.2	0.4	0.0	0.0	0.0	0.0	0.0
Project loans	3.4	2.5	3.6	3.6	3.6	3.6	14.5
Amortization	-1.1	-1.3	-0.2	-0.2	-0.2	-0.2	-0.9
Net domestic	0.3	-3.3	-0.2	0.3	0.5	0.0	0.5
NBT 5/	-0.2	-4.1	-0.3	0.2	0.4	-0.2	0.0
Commercial banks	-0.1	0.1	0.0	0.0	0.0	0.0	0.1
Gross proceeds from privatization	0.5	0.6	0.1	0.1	0.1	0.1	0.4
Other nonbank and discrepancy	0.2	0.1	0.0	0.0	0.0	0.0	0.0
<i>Memorandum items:</i>							
Spending on Social Services	9.4	9.4					10.1
Education	4.0	4.2					4.7
Health	1.3	1.4					1.6
Social Security and Welfare	3.1	2.5					2.7
Other Social Services	1.0	1.3					1.2
Nominal GDP (in millions of somoni)	7,201	9,272	10,867	10,867	10,867	10,867	10,867

Sources: Tajik authorities; and Fund staff estimates.

1/ 2006 extrabudgetary revenue and investment expenditure figures exclude SM17 million recorded as budget revenue and expenditure in the budget for investment projects that have not actually taken place.

2/ 2007 expenditure figure include use of MDRI resources (0.4 percent of GDP) that will mostly be used for the reforms of social protection and to address issues related to health, education, and reform of civil service.

3/ 2006 grants figure includes the MDRI debt relief of 3.5 percent of GDP (\$97.8 million).

4/ 2006 overall balance also excludes the MDRI debt relief that is reflected in grants.

5/ The historical financing figures in this table are based on estimated flows, not differences between end-period stocks.



Table 4. Tajikistan: Accounts of the National Bank of Tajikistan, 2005-07

(End-of-period stock; unless otherwise specified)

	2005	2006			2007			
	Dec. Act 1/	June	Sept. Act 1/	Dec.	March	June	Sept	Dec
(In millions of U.S. dollars; unless otherwise specified)								
Net foreign assets	96	192	186	198	203	214	211	230
Gross assets	231	237	231	252	258	268	266	284
Gross liabilities	135	45	45	55	55	55	55	55
Net international reserves	96	192	186	208	213	224	221	240
Gross assets	231	237	231	252	258	268	266	284
Gross short-term liabilities	135	45	45	45	45	45	45	45
Official exchange rate (Sm/US\$)	3.199	3.281	3.384	3.427	...	...	...	...
Accounting exchange rate (Sm/US\$)	3.427	3.427	3.427	3.427	3.427	3.427	3.427	3.427
(In millions of somoni)								
Net foreign assets	330	657	637	678	696	732	723	787
Gross assets	792	812	790	865	884	919	911	975
Gross liabilities	462	155	153	187	187	187	187	187
Net international reserves	330	657	637	712	730	766	757	821
Gross assets	792	812	790	865	884	919	911	975
Gross short-term liabilities	462	155	153	153	153	153	153	153
Net domestic assets	-22	-344	-296	-315	-376	-360	-320	-357
Net credit to general government of which: MDRI deposits	-232 n.a.	-568 -320	-534 -320	-637 -320	-673 -311	-653 -299	-609 -282	-631 -266
Credit to the private sector	217	212	214	274	246	243	240	237
Other items, net	-7	12	23	48	51	50	48	37
NBT bills	-27	-9	-10	-4	-7	-12	-16	-15
Reserve money	309	313	340	364	320	371	403	430
Currency in circulation	202	217	233	226	197	260	267	246
Bank reserves	103	93	91	134	120	108	132	180
Of which:								
Required reserves	66	65	67	66	72	67	65	75
Somoni	33	31	33	24	24	22	25	30
Foreign exchange	33	34	34	42	49	45	41	44
Other bank deposits	37	28	24	68	47	41	67	105
Somoni	28	26	23	59	...	...	...	...
Foreign exchange	9	2	1	9	...	...	...	...
Other deposits	4	3	16	4	4	4	4	4
Somoni	1	2	2	3	3	3	3	3
Foreign exchange	3	1	14	1	1	1	1	1
(12-month change as a percent of initial reserve money stock)								
Net international reserves	20.5	135.2	114.1	123.8	15.8	34.9	35.4	30.0
Net domestic assets	-11.0	-115.3	-93.2	-94.9	16.1	-5.2	-7.0	-11.6
Reserve money	9.5	19.9	20.9	17.8	19.2	18.8	18.3	18.4

Sources: National Bank of Tajikistan; and Fund staff estimates.

1/ Based on accounting exchange rates: SM3.43=US\$1, SDR 1=US\$1.5, and gold price of US\$635.7 per troy ounce (end-December 2006 rates).

Table 5. Tajikistan: Monetary Survey, 2005–07

(In millions of somoni, end-of-period stock; unless otherwise specified)

	2005		2006			2007			
	Dec.		June	Sept.	Dec.	March	June	Sept.	Dec.
	Act 1/		Act 1/	Act 1/	Est. 1/		Staff Proj. 1/		
Net foreign assets	-151		77	103	243	245	247	205	236
National Bank of Tajikistan	330		657	637	678	696	732	723	787
Commercial banks	-481		-580	-534	-435	-451	-484	-518	-551
Net domestic assets	885		720	761	625	650	677	760	792
Net credit to general government	-267		-611	-583	-703	-737	-716	-667	-686
Credit to the private sector	1,352		1,523	1,548	1,520	1,574	1,563	1,616	1,679
o/w cotton	660		660	664	665	665	665	665	665
Other items, net	-201		-193	-204	-192	-187	-171	-189	-201
Broad money	578		684	765	786	814	843	884	947
Somoni broad money	297		344	360	370	383	396	416	445
Currency outside banks	156		170	192	196	176	205	202	182
Deposits	140		174	168	174	207	191	214	263
Foreign currency deposits	281		340	405	417	431	446	468	501
Bills payable 2/	156		112	100	81	81	81	81	81
<i>Memorandum items:</i>									
Official/accounting exchange rate (Sm/US\$, eop)	3.199		3.281	3.427	3.427	3.427	3.427	3.427	3.427
Broad money (12-month percent change)	23.7		32.4	30.3	36.1	53.3	23.2	15.7	20.4
Credit to the private sector (12-month percent change)	14.6		21.8	19.0	12.4	11.0	2.6	4.4	10.4
Year-to-year average of quarterly velocity 3/	3.4		3.3	3.4	3.3	3.2	3.1	3.1	3.1
Money multiplier 4/	1.87		2.19	2.25	2.16	2.54	2.27	2.20	2.20

Sources: National Bank of Tajikistan; and Fund staff estimates.

1/ Based on accounting exchange rates: SM3.43=US\$1, SDR 1=US\$1.5, and gold price of US\$635.7 per troy ounce (end-December 2006 rates).

2/ Liabilities to cotton financiers related to domestic cotton financing.

3/ Quarterly GDP divided by end-quarter broad money; four-quarter average.

4/ Broad money divided by reserve money.

Table 6. Tajikistan: Medium-Term Balance of Payments, 2005-11

(In millions of US dollars)

	2005	2006	2007	2008	2009	2010	2011
						Staff Projections	
Current account	-58	-70	-476	-528	-423	-169	-184
Balance on goods and services 1/	-620	-978	-1,595	-1,728	-1,697	-1,506	-1,583
Balance on goods	-622	-986	-1,477	-1,597	-1,618	-1,531	-1,622
Exports	346	350	383	416	462	534	563
Imports	-968	-1,336	-1,860	-2,013	-2,080	-2,065	-2,185
<i>Of which: projects financed by China</i>	...	...	-256	-294	-203	...	...
Balance on services	2	8	-118	-131	-79	25	39
<i>Of which: aluminium tolling fee</i>	116	168	184	203	227	250	275
<i>Of which: projects financed by China</i>	...	...	-85	-98	-68	...	...
Balance on income	-75	-99	-105	-113	-117	-116	-120
Balance on transfers	636	1,007	1,223	1,313	1,391	1,453	1,519
<i>Of which: migrants' remittances, net</i>	526	898	1,123	1,221	1,305	1,372	1,442
Capital and financial account	83	182	508	578	493	241	221
Capital transfers	19	126	40	31	18	17	18
<i>Of which: MDRI debt relief</i>	...	99	...	...	...	...	...
Public sector (net)	48	45	410	486	395	130	79
Disbursements 2/	86	82	454	531	429	168	186
<i>Of which: projects financed by China</i>	...	...	341	391	271	...	...
Amortization	-38	-37	-44	-45	-34	-37	-108
FDI	55	66	70	80	87	94	115
Commercial bank NFA (- increase)	18	-24	32	...	...	...	...
Electricity credit	6	18	...	...	...	...	...
Other short-term capital 3/	-61	-49	-44	-18	-7	...	10
Errors and omissions	-1	...	...	...	...	...	...
Overall balance	25	112	32	50	70	71	37
Use of international reserves (- increase)	-41	-28	-32	-50	-70	-70	-30
Financing items	16	-84	...	...	...	-1	-7
IMF (net)	15	-85	...	...	...	-1	-7
Purchases/disbursements	29	14	...	...	...	...	...
Repurchases/repayments	14	99	...	...	...	1	7
Financing gap	...	...	...	...	...	...	...
In percent of GDP	...	...	...	...	...	...	...
<i>Memorandum items:</i>							
GDP (in millions of U.S. dollars)	2,311	2,811	3,141	3,457	3,806	4,189	4,656
Current account balance in percent of GDP	-2.5	-2.5	-15.2	-15.3	-11.1	-4.0	-3.9
Current account balance excluding projects financed by China	-2.5	-2.5	-4.3	-4.0	-4.0	-4.0	-3.9
Gross reserves	224	252	284	334	404	474	504
(in months of imports) 4/	2.1	2.0	2.1	2.3	2.5	2.8	2.8
Debt service on PPG external debt 5/	60	46	62	68	61	67	145
(in percent of exports of goods)	17.4	13.1	16.2	16.4	13.2	12.6	25.7
Total PPG external sector debt	887	859	1,265	1,746	2,137	2,273	2,350
(in percent of GDP)	38.4	30.6	40.3	50.5	56.2	54.2	50.5

Sources: Tajik authorities; and Fund staff estimates.

1/ Starting from 2005, the export and import figures reflect the transition to tolling arrangement for aluminum exports.

2/ Besides China, main official creditors of Tajikistan are Asian Development Bank, International Development Association, and Islamic Development Bank.

3/ Includes accumulation of foreign currency balances by residents of Tajikistan.

4/ Excluding electricity, which is on barter basis, and imports related to projects financed by loans from China.

5/ Data for 2006 exclude \$99.2 mln. IMF repurchase under MDRI assistance.

Table 7. Tajikistan: Medium-Term Macroeconomic Projections, 2004–11

	2004	2005	2006	2007	2008	2009	2010	2011
			Staff Projections					
National income and prices								
Nominal GDP (in millions of somoni)	6,158	7,201	9,272	10,867	12,441	14,242	16,304	18,665
Nominal GDP (in millions of U.S. dollars)	2,073	2,311	2,811	3,141	3,457	3,806	4,189	4,656
Real GDP (annual percent change)	10.6	6.7	7.0	7.5	8.0	8.0	8.0	8.0
GDP per capita (in U.S. dollars)	324	357	430	475	517	563	613	674
GDP deflator (annual percent change)	17.0	9.6	20.3	9.0	6.0	6.0	6.0	6.0
Consumer prices (12-month percent change, e.o.p.)	5.7	7.1	12.7	9.0	6.0	6.0	6.0	6.0
			(In percent of GDP)					
General government finances								
Total revenue and grants	17.9	20.1	23.4	20.7	20.3	20.1	20.3	20.2
<i>Of which:</i>								
Tax revenue	15.2	16.6	16.5	16.5	16.9	17.1	17.4	17.4
Total expenditure	20.3	23.0	21.7	34.8	35.6	31.3	24.4	24.5
<i>Of which:</i>								
Current expenditure	12.1	15.1	15.0	15.9	16.2	16.5	16.9	17.0
Externally-financed public investment program (PIP)	3.1	3.4	3.1	15.7	16.3	11.8	4.4	4.4
Fiscal balance (excluding the PIP) 1/	0.7	0.5	0.8	0.4	0.1	0.0	-0.1	-0.2
			(In percent of GDP)					
Savings/investment balances								
External current account balance	-3.9	-2.5	-2.5	-15.2	-15.3	-11.1	-4.0	-4.1
Overall fiscal balance (including the PIP) 1/	-2.4	-2.9	-1.8	-14.1	-15.3	-11.3	-4.1	-4.2
Net savings (S-I) of the private sector 2/	-1.6	0.4	-0.7	-1.1	0.0	0.2	0.1	0.1
			(In millions of U.S. dollars, unless otherwise indicated)					
External sector 3/								
Exports of goods and services	1,211	601	668	734	803	893	1,009	1,088
Imports of goods and services	1,451	1,221	1,646	2,329	2,531	2,590	2,515	2,680
Current account balance	-82	-58	-70	-476	-528	-423	-169	-193
Gross international reserves	189	224	252	284	334	404	474	524
Gross international reserves, excl. bartered electricity and imports financed by loans from China (in months of imports)	...	2.1	2.0	2.1	2.3	2.5	2.8	2.9

Sources: Tajik authorities; and Fund staff estimates.

1/ Fiscal balance for 2007-10 includes MDRI spending of about 0.5 percent of GDP. Overall fiscal balance in 2006 excludes the MDRI debt relief of 3.5 percent of GDP.

2/ Defined as the external current account balance less the overall fiscal balance (including the PIP).

3/ Starting from 2005, exports and imports figures reflect transition to tolling arrangement for aluminum exports. Therefore, they show a sudden drop compared to earlier years.

Table 8. Tajikistan: Indicators of External Vulnerability, 2002–06

(In units indicated)

	2002	2003	2004	2005	2006
<b>Financial indicators</b>					
Broad money (percent change)	42.9	28.6	14.1	23.9	40.6
Private sector credit (percent change)	20.2	10.9	57.9	18.3	17.0
31 day treasury bill yield (percent) 1/	23.1	4.9	6.2	7.0	10.7
<b>External indicators</b>					
Exports of goods and services (in U.S. dollars, percent change)	9	23	23	...	11
Imports of goods and services (in U.S. dollars, percent change)	10	23	27	...	35
Current account balance (in millions of U.S. dollars)	-43	-20	-82	-58	-70
Capital and financial account balance (in millions of U.S. dollars)	3	55	105	83	182
Gross official reserves (in millions of U.S. dollars)	96	135	189	224	252
Central bank short-term foreign liabilities (in millions of U.S. dollars)	...	...	...	...	...
Official reserves (in months of relevant imports)	1.6	1.8	2.5	2.0	2.0
Ratio of broad money to reserves	1.1	1.0	0.8	0.8	0.9
Total external debt (in millions of U.S. dollars) 2/	...	...	...	1,166	1,150
<i>Of which:</i> Public and publicly guaranteed debt	944	990	824	887	859
Ratio of total external debt to exports of goods and services 3/	...	...	...	2.1	1.9
Public sector external interest payments (as a percent of exports goods and services) 3/	2.6	3.0	1.5	1.6	1.5
Public sector external amortization payments (as a percent of exports of goods and services) 3/ 4/	10.1	5.4	32.4	9.5	22.6
Exchange rate (In somoni per U.S. dollar, period average)	2.8	3.1	3.0	3.1	3.3

Sources: Tajik authorities; and Fund staff estimates.

1/ 2003–06 end-period rate on 28-day NBT certificate.

2/ No reliable data are available on the external debt of the private sector before 2005.

3/ Including debt service to the IMF; exports of goods and services excluding electricity traded on a barter basis.

4/ High ratio in 2004 reflects \$250 mln debt-equity swap with Russia, included in amortization data.

Table 9. Tajikistan: Financial Soundness Indicators, 2003–06  
(In percent, unless otherwise indicated)

	2003	2004	2005	2006
<b>Capital adequacy</b>				
Tier I capital as percent of risk-weighted assets	...	38.7	34.2	26.8
Reported total capital to risk weighted assets (K1-1)	-3	44.7	37.9	29.9
<b>Asset quality 1/</b>				
Nonperforming loans to gross loans	71.5	20.6	14.3	11.3
excluding Agroinvestbank	11.5	n.a.	n.a.	n.a.
Nonperforming loans net of provisions to capital	2.3	19.3	16.1	19.1
Provisions to nonperforming loans	89.9	47.2	36.8	24.7
Banks exceeding maximum single borrower limit 2/	6 of 14	3 of 12	2 of 12	1 of 10
<b>Earnings and profitability</b>				
Reported return on assets (ROA)	10.6	2.9	4.7	3.8
Reported return on equity (ROE)	1.4	10.2	17.2	15.8
Interest margin to gross income	10.9	42.7	48.2	47.5
Noninterest expenditures to gross income	46.1	61	55.2	62.9
Salary expenditures to non-interest expenditures	28.2	25.8	27.1	22
<b>Liquidity</b>				
Liquid assets to total assets	22.1	36.9	30	35.9
Liquid assets to demand and savings deposits	124.7	113.5	80.2	75.6
Liquid assets to total deposits	75.6	71.2	54.9	56.6
<b>Sensitivity to market risk</b>				
Net open position in foreign exchange to capital	n.a.	36.3 long	8.8 long	5.1 long

Sources: National Bank of Tajikistan; and Fund staff estimates.

1/ Nonperforming loans include three loan classifications: watch, doubtful, and loss.

2/ Maximum single borrower limit is defined as 25 percent of capital (K3-1).

Table 10. Tajikistan: Millennium Development Goals

	1990	1995	2004	2005	2006	2015 Target
<b>Goal 1. Eradicate extreme poverty and hunger</b>						
Target 1: Halve, between 1990 and 2015, the proportion of people whose income is less than one dollar a day.						
1. Population below \$1 a day (percent)	...	...	...	...	...	...
1a. Population below \$2 a day (percent) 1/	...	...	57.0	...	...	41.0
2. Poverty gap at \$1 a day (percent)	...	...	...	...	...	...
3. Percentage share of income or consumption held by poorest 20 percent	...	...	...	...	...	...
Target 2: Halve, between 1990 and 2015, the proportion of people who suffer from hunger.						
4. Prevalence of child malnutrition (percent of children under 5)	...	...	...	...	...	...
5. Population below minimum level of dietary energy consumption (percent)	...	...	...	...	...	...
<b>Goal 2. Achieve universal primary education</b>						
Target 3: Ensure that, by 2015, children everywhere, boys and girls alike, will be able to complete a full course of primary schooling.						
6. Net primary enrollment ratio (percent of relevant age group)	...	...	96.7	...	...	100.0
7. Percentage of cohort reaching grade 5 (percent)	...	...	...	...	...	100.0
8. Youth literacy rate (percent ages 15–24)	99.8	...	99.8	...	...	100.0
<b>Goal 3. Promote gender equality</b>						
Target 4: Eliminate gender disparity in primary and secondary education preferably by 2005 and to all levels of education no later than 2015.						
9a. Ratio of girls to boys in primary education (percent)	...	...	95.0	...	...	100.0
9b. Ratio of girls to boys in secondary education (percent)	...	...	84.0	...	...	100.0
9c. Ratio of girls to boys in tertiary education (percent)	...	...	33.0	...	...	...
10. Ratio of young literate females to males (percent ages 15–24)	100.0	...	100.0	...	...	100.0
11. Share of women employed in the nonagricultural sector (percent)	39.3	44.0	53.3	...	...	...
12. Proportion of seats held by women in national parliament (percent)	...	...	12.7	12.7	17.5	...
<b>Goal 4. Reduce child mortality</b>						
Target 5: Reduce by two-thirds, between 1990 and 2015, the under-five mortality rate.						
13. Under 5 mortality rate (per 1,000)	128.0	123.0	118.0	...	...	42.3
14. Infant mortality rate (per 1,000 live births)	99.0	95.0	91.0	...	...	30.7
15. Immunization, measles (percent of children under 12 months)	...	88.0	89.0	...	...	100.0
<b>Goal 5. Improve maternal health</b>						
Target 6: Reduce by three-quarters, between 1990 and 2015, the maternal mortality ratio.						
16. Maternal mortality ratio (modeled estimate, per 100,000 live births)	130.0	120.0	...	...	...	30.0
17. Births attended by skilled health staff (percent of total)	...	...	...	...	...	100.0
<b>Goal 6. Combat HIV/AIDS, malaria and other diseases</b>						
Target 7: Have halted by 2015, and begun to reverse, the spread of HIV/AIDS. Have halted by 2015, and begun to reverse, the incidence of malaria and other major diseases.						
18. People living with HIV, 15-49 years old, percentage	...	...	...	0.1	...	...
19. Contraceptive prevalence rate (percent of women ages 15–49)	...	...	...	...	...	...
20. Number of children orphaned by HIV/AIDS	...	...	...	...	...	...
Target 8: Have halted by 2015, and begun to reverse, the incidence of malaria and other major diseases.						
21. Incidence of tuberculosis (per 100,000 people)	195.0	...	277.0	...	...	...
22. Tuberculosis cases detected under DOTS (percent)	...	...	11.7	...	...	...

Table 10 (concluded). Tajikistan: Millennium Development Goals

	1990	1995	2004	2005	2006	2015 Target
<b>Goal 7. Ensure environmental sustainability</b>						
Target 9: Integrate the principles of sustainable development into country policies and programs and reverse the loss of environmental resources.						
23. Forest area (percent of total land area)	2.9	...	...	2.9	...	...
24. Nationally protected areas (percent of total land area)	6.8	18.2	18.2	18.2	...	...
25. Energy use (Kg oil equivalent) per \$1,000 (PPP) GDP	807	684	...	...	...	...
26. CO2 emissions (metric tons per capita)	...	0.90	0.00	...	...	...
Target 10: Halve, by 2015, the proportion of people without sustainable access to safe drinking water.						
27. Access to an improved water source (percent of population)	...	...	59.0	...	...	...
Target 11. Achieve by 2020 significant improvement for at least 100 million slum dwellers.						
28. Access to improved sanitation (percent of population)	...	...	51.0	...	...	...
29. Access to secure tenure (percent of population)	...	...	...	...	...	...
<b>Goal 8. Develop a Global Partnership for Development</b>						
Target 12: Develop and implement strategies for decent and productive work for youth.						
30. Youth unemployment rate (percent of total labor force ages 15–24)	...	...	...	...	...	...
Target 13: Develop further an open, rule-based, predictable, non-discriminatory trading and financial system. Address the Special Needs of the Least Developed Countries. Address the Special Needs of landlocked countries and small island developing states.						
32. Fixed line and mobile telephones (per 1,000 people)	45.4	45.0	...	...	...	...
33. Personal computers (per 1,000 people)	...	...	...	...	...	...
33a. Internet users (per 1,000 people)	...	...	0.1	...	...	...

Sources: World Bank; United Nations - <http://unstats.un.org/unsd/mdg/Data.aspx?cr=762>.

1/World Bank estimate based on purchasing power parity expenditure level of \$2.15 per day.



## APPENDIX I. TAJIKISTAN: JOINT FUND–WORLD BANK EXTERNAL DEBT SUSTAINABILITY ANALYSIS

*This DSA updates the previous DSA prepared in early 2006 (Country Report No. 06/63). Since then, Tajikistan has received debt relief from the IMF under the MDRI (SDR 69.3 million), and contracted \$604 million of debt from China to finance projects in the infrastructure and energy sectors. In addition, the government of Tajikistan intends to contract \$400 million of debt from China to build new hydroelectric power stations. Therefore, despite the MDRI relief, debt distress risk has increased significantly and could be now classified as high. Under the baseline scenario, the ratios of NPV of debt to GDP, exports, and revenue breach their policy-dependent thresholds in the medium term, although they improve over time. The ratio of NPV of debt to exports, however, is projected to remain above the threshold throughout the projected period. The breach of the thresholds is more severe under stress tests reflecting potential macroeconomic shocks, including falling short of projected growth, and additional significant borrowing. The ratios for debt service payments to exports and revenue are expected to remain below the thresholds under the baseline scenario. However, under stress tests and alternative scenarios, these ratios would also breach the thresholds.*

### Data and Methodology<sup>1</sup>

1. **The DSA focuses mainly on external public and publicly guaranteed (PPG) debt.** Government and government guaranteed debt includes debt directly contracted or guaranteed by the government,<sup>2</sup> and partially includes public sector nonguaranteed debt.<sup>3</sup> To the extent that the information on the stock of private debt is available from the authorities (in 2005 the NBT started compiling inventory of external private sector debt not guaranteed by the government), it is incorporated into the DSA. As for domestic debt, domestic securitized public debt stands at \$53 million and consists of government securities of \$47 million held

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<sup>1</sup> This DSA was conducted jointly by Fund and World Bank staff and in collaboration with the authorities, using the debt sustainability framework for low-income countries. It has benefited from Fund and Bank staff consultations with the Ministry of Finance (MoF) during missions to Dushanbe in October–November 2006 and January 2007, and included a full reconciliation of debt data. The Low-Income Countries (LICs) DSA uses (a) the current year exports as denominators for estimating debt-to-exports ratio; (b) the WEO exchange rate projections for estimating debt stocks and debt service; and (c) a 5 percent discount rate.

<sup>2</sup> Tajikistan has some “disputed” government guaranteed debt from the period prior to 1998, when guarantees were issued in ad hoc manner; the estimated amount of guarantees is about \$50 million. In 1999, the issuance of guarantees was centralized at the MoF. The disputed guarantees were not included in the DSA given that exact terms, conditions, and government repayment obligations were not known at the time of this analysis. However, even if these guarantees were recognized as valid, given the small amount involved (about 6 percent of total public and publicly guaranteed debt at end-2006), including them in the DSA would not materially change the main results.

<sup>3</sup> Coverage of public sector nonguaranteed debt is limited to debt on which debt service is likely to be assumed by the government.

by the NBT and government guarantees to finance the cotton sector of \$7 million.<sup>4</sup> At present, given its small size, incorporating domestic debt into the analysis will not materially affect the results of the DSA. However, in the future, the evolution of public domestic debt will need to be monitored closely with the view to incorporating it into the DSA.

## II. Tajikistan's External Debt Situation

2. **Tajikistan has continued to meet its external debt obligations on a timely basis, while seeking relief from its creditors.** Since a large share of loans has been provided on a concessional basis, debt service obligations remain manageable. In 2006, Tajikistan obtained rescheduling of debt from Iran—no debt service payments are expected until 2008 on a \$25 million loan, and maturity was extended by two years to 9 years—and Uzbekistan—\$8 million of debt service payment in 2006 and 2007 were rescheduled to 2008.

3. **Debt relief under MDRI and the contracting of loans from China were two major developments in 2006 that affected the external debt situation in Tajikistan.** In January 2006, Tajikistan qualified for debt relief from the IMF under MDRI and was granted debt relief amounting to SDR 69.3 million (\$100 million).<sup>5</sup> Following debt relief, however, Tajikistan contracted debt from China in the amount of \$604 million to finance projects in the infrastructure and energy sectors.<sup>6</sup> While the debt was granted on concessional terms, with a 40 percent grant element, its size (25 percent of 2006 GDP) and uncertainty regarding the economic impact of the projects increased risks to debt sustainability.<sup>7</sup> However, with no disbursement on loans from China in 2006, the nominal PPG debt-to-GDP ratio continued to decline, reaching 31 percent at the end of the year mainly on account of strong GDP growth and debt relief.

4. **In 2007, the contracting of an additional \$400 million of debt from China is expected to increase risk of debt problems in the medium term.** The authorities have indicated that they are pursuing additional financing from China for the construction of new hydropower plants. While concessional terms are expected, the exact details of financing agreement have not been worked out yet. Regardless of the terms, the rapid accumulation of

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<sup>4</sup> However, given the large size of government deposits at the NBT, the NBT remains a net debtor to the government.

<sup>5</sup> Debt relief was granted on the basis that Tajikistan's income per capita was below \$380 in 2004. Under MDRI, Tajikistan was provided debt relief on the stock of outstanding debt as of end-2004.

<sup>6</sup> \$281.2 million loan was contracted by the government to finance the construction of the road connecting Dushanbe and the northern part of Tajikistan. Two loans—\$267.2 million for construction of a North-South electricity transmission line and \$58.1 million for construction of Lolazor-Khatlon electricity transmission lines—were contracted for on-lending to Barki Tajik, which is expected to service the debt.

<sup>7</sup> While preliminary indications are that the projects will increase Tajikistan's growth and export potential, a thorough analysis to assess the economic impact of the projects has not been undertaken yet.

debt will further increase risks to debt sustainability (see the baseline scenario). It is estimated that following the disbursement of loans from China, the nominal PPG debt-to-GDP ratio will increase to 57 percent of GDP by 2009, or by 26 percentage points in three years, remaining, however, below its 2000 level of 96 percent.

5. **A potential bail out of the cotton sector by the government poses additional risk to debt sustainability.** Political pressure has been building up to provide financing to agriculture (cotton sector), as reflected in the recent decision by the NBT to contract \$10 million debt from China for on-lending to agriculture. By various estimates, the debt accumulated by the cotton sector ranges between \$90 and \$300 million. While the resolution of the debt issue has been on the agenda of the government, no clear-cut solution has emerged yet. Given that the government assigns high social importance to the cotton sector, there is a probability that the government will assume the debt, at least partially, or will subsidize future lending to the sector. This DSA tests the worst case scenario under which the government assumes \$300 million.<sup>8</sup>

### III. Baseline Scenario

6. **The baseline scenario, developed on a realistic set of assumptions about economic policies and outcomes (Box 1), shows that Tajikistan's debt is sustainable, but is at a high risk of debt distress.** According to the latest three-year average World Bank's CPIA rating, Tajikistan's policies and institutions are assessed as those corresponding to a "poor performer."<sup>9</sup> The debt-burden thresholds for countries in this category are (a) NPV of debt-to-exports of goods and services of 100 percent; (b) NPV of debt-to-GDP of 30 percent; and (c) NPV of debt-to-fiscal revenue of 200 percent. The relevant debt service thresholds are (a) 15 percent of exports of goods and services; and (b) 25 percent of revenues.

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<sup>8</sup> Although this is an unlikely scenario, this could also be a proxy for a stress test for additional concessional lending.

<sup>9</sup> The three-year average of CPIA ratings is used according to recently issued guidelines on DSA for LIC. These guidelines aim at a more conservative and less volatile assessment of risk than that based on a single latest CPIA rating. For Tajikistan, however, the use of the latest CPIA ratings would not substantially change the assessment of risk in this DSA. Indeed, according to the latest 2005 CPIA rating, Tajikistan is placed into a "medium performer" category implying higher policy dependent thresholds. However, even these thresholds are breached in the medium term—albeit by a smaller margin—pointing to increased risk to debt sustainability.

### Box 1. Tajikistan: Macroeconomic Assumptions

**Real GDP** is projected to grow at about 8 percent per year until 2011, and at 6.5 percent between 2012 and 2026. This figure is slightly above its ten-year historical average of 6.1 percent, but well below its latest five-year (post-Russian crisis) average of 9.4 percent. Growth is driven by exports, FDI, and expanding nontraditional sectors (services, textiles, and noncotton agriculture), as well as continued inflows of remittances.

**Exports of goods and services** are projected to grow at a rate of 10 percent through 2012, reflecting expansion in nontraditional sectors and strong external demand, and at 7 percent thereafter as the economy will be expanding following large investments in the energy sector, and in response to a stable macroeconomic environment and significant progress with structural reforms.

**The current account** deficit is expected to deteriorate sharply in 2007–2009 due to the increase in imports financed by loans from China, but will improve in 2010 following the completion of the projects. Thereafter, the current account deficit is expected to remain at about 4 percent as imports and exports are expected to grow at the same pace and financing will be constrained to official financing on concessional terms and stable FDI inflows. The net foreign transfer inflows (driven by remittances) are assumed to remain strong but decline from 36 to 20 percent of GDP from 2006 to 2026. The **reserve coverage** of imports is projected to build up gradually to three months of imports by 2026.

**The fiscal stance** continues to be prudent. During 2006–2010, revenues excluding grants will increase from 19.3 to 19.5 percent of GDP, and then further to 21 percent by 2026. Expenditure, excluding foreign-financed PIP, will increase at the same pace leaving the fiscal deficit broadly unchanged.

**Official external loan financing (on concessional terms)** is projected to peak at 15.4 percent of GDP in 2008 and then decline to 4 percent by 2010 and remain at that level thereafter.

7. **Under the baseline scenario, three of Tajikistan’s external debt burden indicators are projected to breach policy-dependent thresholds following the rapid disbursement of loans from China (Table 1 and Figure 1).** In particular, by 2009 the NPV of debt-to-exports of goods and services ratio will reach 186 percent, exceeding the threshold of 100 percent by a significant margin. The NPV of debt-to-GDP will be at 44 percent, also significantly exceeding the 30 percent threshold, and NPV of debt-to-revenue will reach 227 percent exceeding the 200 percent threshold as well. By 2026, however, these ratios are expected to decline to 136, 23, and 107 percent, respectively. The NPV of debt-to-export ratio, however, while on a declining path, will remain above its threshold over the years, underscoring the importance of implementing the relevant structural reforms targeted at increasing the GDP and export potential of Tajikistan.<sup>10</sup>

8. **External debt service ratios are expected to stay below their thresholds over the entire period.** During the projected period, debt service payments continue to be manageable, with the assumption that all of Tajikistan’s external public and publicly guaranteed debt has been contracted on concessional terms, albeit spiking during the years when principal payments on loans from China fall due. In particular, the debt service-to-revenue ratio would remain comfortably below 25 percent, peaking in 2014 at 17 percent

<sup>10</sup> Substantially lower than projected net foreign transfer inflows in the outer years (for example, due to a deteriorating regional economic situation) would likely lower imports, exports, and real GDP growth, with a possibility of the NPV of debt-to-export ratio marginally exceeding its policy-relevant threshold in those years.

and declining thereafter to 11 percent. The debt service-to-export ratio will peak at 14 percent (slightly below the 15 percent threshold), but then decline to 6 percent.

#### IV. Alternative Scenarios and Bound Tests

9. **The historical scenario is based on averages from 1998 to 2005, and thus reflects a period of macroeconomic consolidation, some progress with structural reforms, and debt reduction.**<sup>11</sup> During 1998–2005, the current account deficit was relatively small as financing was limited, and growth was high as the economy was growing from a low level. Therefore, under this scenario, not only do all debt burden ratios remain well below the threshold indicators, they also follow a downward trend throughout the projection period. While the scenario illustrates the importance of preserving macroeconomic stability, progress with structural reforms and continued prudent debt management, the scenario is not very useful as a benchmark against which the current debt situation can be assessed because both the conditions of the economy and its external environment have changed dramatically.

10. **A scenario incorporating an additional \$300 million borrowing on concessional terms in 2007 to bail out the cotton sector shows increased risk of debt distress compared to the baseline scenario.** In particular, all ratios, except the one for debt service-to-revenue, will breach their respective thresholds. The ratios of NPV of debt to GDP, exports, and revenue follow the baseline pattern, but exceed the thresholds sooner and by higher margin compared to the baseline scenario. The ratio of debt service-to-exports breaches its 15 percent threshold in 2012–13, but then declines by the end of the projection period (Table 2 and Figure 1).

11. **A high-investment low-growth scenario underscores the risk to debt sustainability of the current debt-based development strategy.** Rapid accumulation of debt together with uncertainty regarding the impact of investments financed by China on growth tests the robustness of the conclusions of the baseline scenario. This alternative scenario shows that if growth were to come at half the rate forecasted by the authorities, all ratios, except for the debt service-to-revenue, will breach and remain above or very close to their respective thresholds. Moreover, the ratio of NPV of debt-to-export increases and becomes unsustainable (Table 3 and Figure 1).

12. **A relaxation of the authorities' current prudent approach to contracting external debt only on concessional terms, would lead to a deterioration of Tajikistan's external debt indicators compared to the baseline scenario.** If all new borrowing were to be contracted on less than concessional terms during the projection period, Tajikistan's NPV debt-to-GDP ratio would rise substantially. Specifically, with the increase in the

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<sup>11</sup> The 1995–97 period has been excluded from historical average scenario due to disruptions from civil war. The average values for the 1998–2005 period are calculated for current account deficit, real GDP growth, GDP deflator in \$ terms, export growth, net transfers and FDI to GDP ratios.

average interest rate on new disbursements by 2 percentage points, the NPV of debt-to-GDP ratio would rise to 50 percent by 2009 and slowly decline afterwards to 34 percent by 2026 remaining above 30 percent threshold throughout the projected period. The ratios of NPV of debt-to-exports and debt service-to-exports would peak at 215 and 19 percent, respectively, and remain above their thresholds at a roughly steady level during the projected period. The NPV of debt-to-revenue ratio will peak at 261 percent in 2009, but then decline to 162 percent at the end of the projected period (Table 4 and Figure 1).

13. **Bound tests show that adverse macroeconomic shocks would also have a profound negative impact on Tajikistan’s external position.** In the event of a combined shock (to real GDP growth, exports growth, FDI inflows), all ratios would exceed the policy-dependent thresholds by a significant margin. In particular, Tajikistan’s NPV of debt-to-GDP ratio would rise to 109 percent by 2009, falling below the policy-dependent threshold of 30 percent only by 2026. The same shock would also significantly worsen the NPV of debt-to-revenues ratio, which would jump to 565 percent in 2009 and stay above the threshold of 200 percent until 2022.<sup>12</sup> The ratios of the NPV of debt-to exports and debt service-to-exports would peak at 531 and 44 percent, respectively, and while on a declining path, would remain above the thresholds throughout the projected period. Debt service-to-revenue ratio would also exceed the threshold between 2013 and 2022, but would decline below the threshold after 2022.

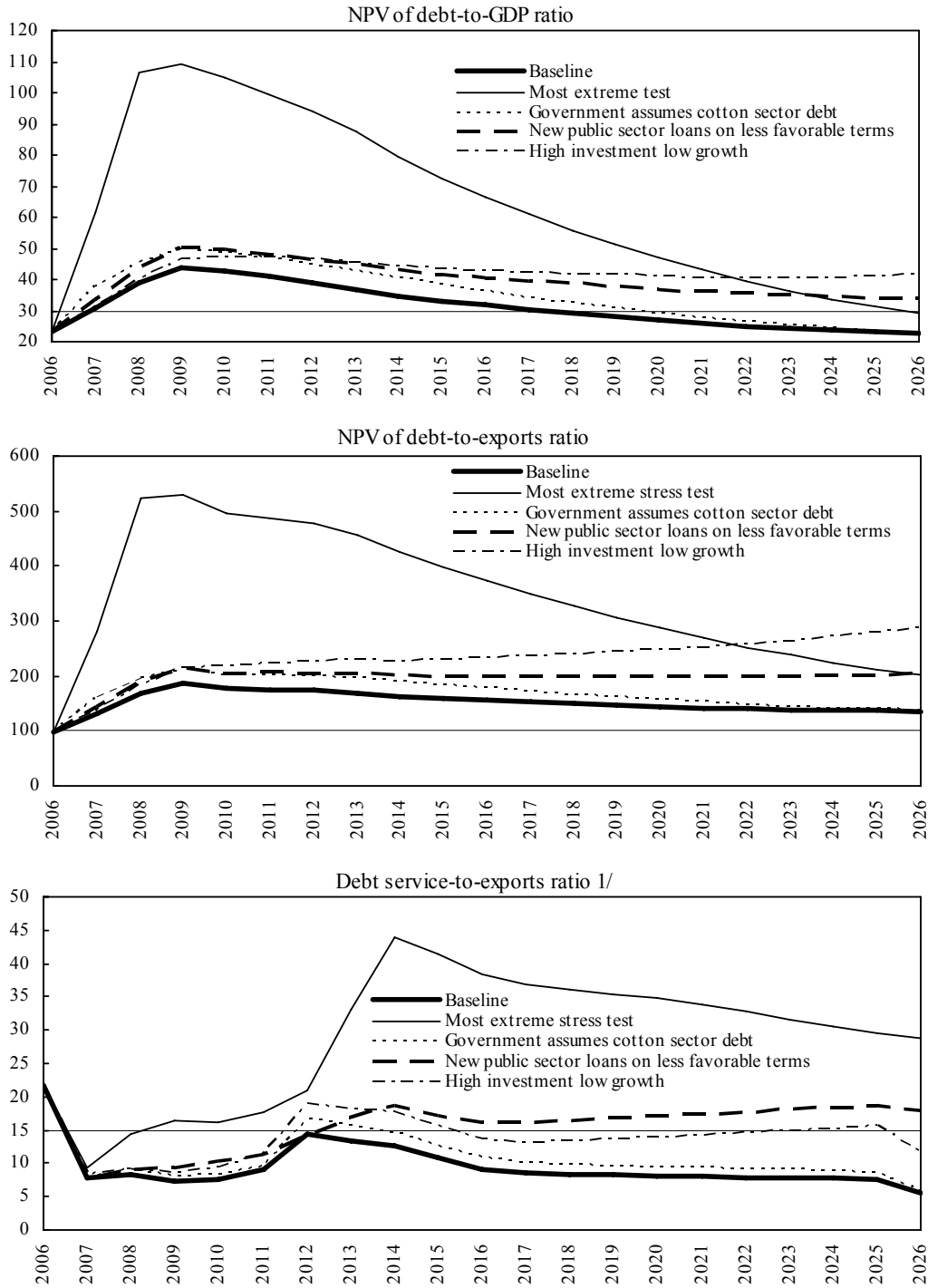
## VI. Conclusions

14. **Tajikistan’s risk of debt distress has increased significantly and has become high.** The results of the alternative scenarios and stress tests indicate that the debt sustainability situation could further deteriorate with negative macroeconomic shocks, borrowing on nonconcessional terms, or incurring extra debt—even on concessional terms—in an attempt to bail out the agricultural sector, and could become unsustainable if growth associated with large prospective investments does not materialize. The DSA results thus underscore the need for the authorities to exercise extreme caution in incurring extra debt and vetting projects, strengthening their debt management capacity, including developing “in house” capacity to conduct DSA, and making sure that external resources are used productively. Sound macroeconomic policies and the acceleration of structural reforms, especially in the agricultural and electricity sectors, would also be essential for maintaining debt sustainability. By contributing to higher export and output growth, these measures would reduce Tajikistan’s vulnerability to exogenous shocks.

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<sup>12</sup> Since Tajikistan is a small open economy with a high share of exports-to-GDP, the debt-to-revenue indicator is an important measure of debt vulnerabilities.

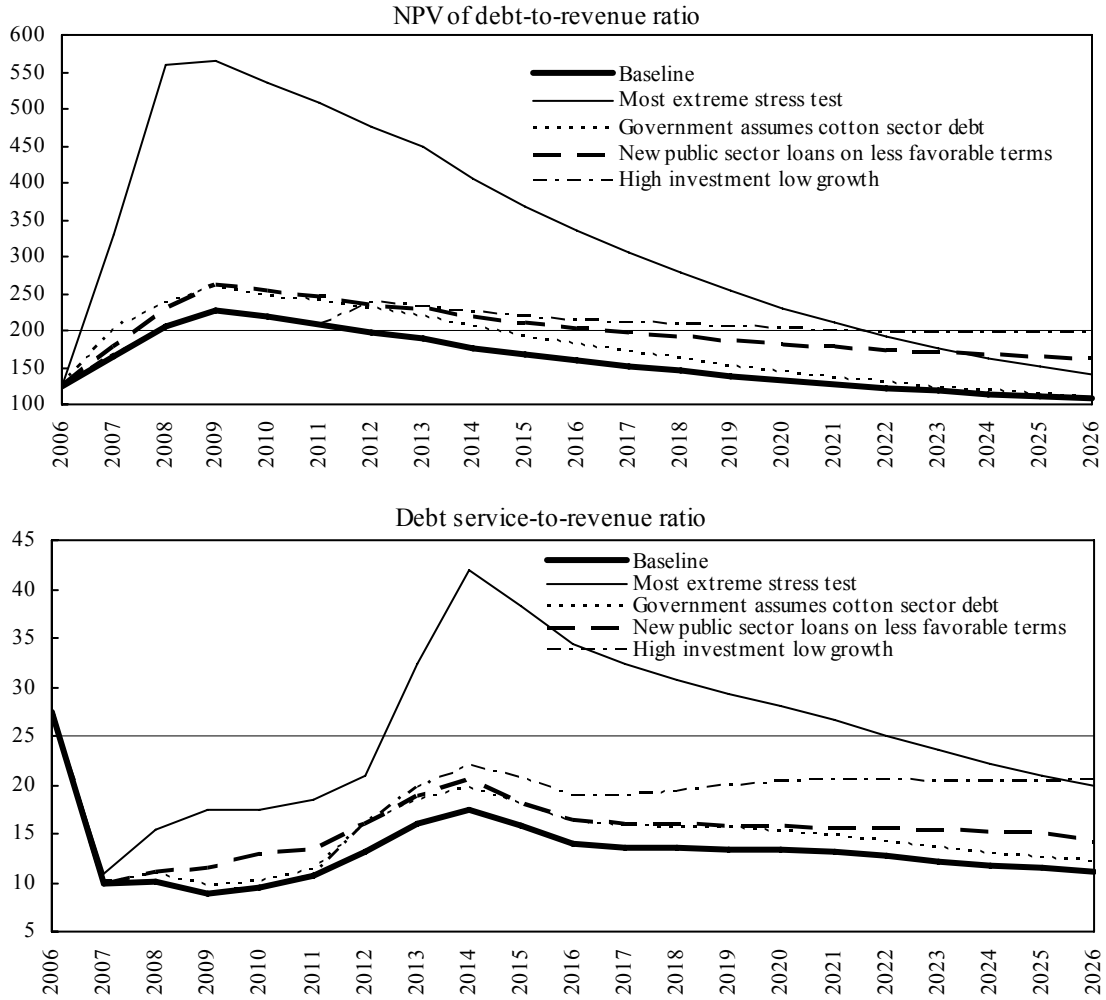
Figure 1. Tajikistan: Indicators of Public and Publicly Guaranteed External Debt Under Alternative Scenarios, 2006-2026  
(In percent)



Source: Staff projections and simulations.

1/ Spike in the ratio in 2006 reflects debt service to the IMF financed under MDRI.

Figure 1. Tajikistan: Indicators of Public and Publicly Guaranteed External Debt Under Alternative Scenarios, 2006-2026 (Concluded)  
(In percent)



Source: Staff projections and simulations.



Table 1. Tajikistan: External Debt Sustainability Framework, Baseline Scenario, 2006-2026 1/  
(In percent of GDP, unless otherwise indicated)

	Actual					Historical		Projections											2012-26	
	2002	2003	2004	2005	2005	Average 6/	Standard Deviation 6/	2006	2007	2008	2009	2010	2011	2006-11		2012-26				
															Average	Average				
<b>External debt (nominal) 1/</b>	106.3	83.5	55.3	50.4	50.4			40.9	49.4	58.7	63.6	60.9	56.4	44.8	38.1					
o/w public and publicly guaranteed (PPG)	78.9	63.7	39.7	38.4	38.4			30.6	40.3	50.5	56.2	54.2	50.5	41.3	36.9					
Change in external debt	-16.3	-22.8	-28.2	-4.8	-4.8			-9.6	8.5	9.3	4.8	-2.7	-4.5	-1.2	0.1					
Identified net debt-creating flows	-0.9	-3.4	1.0	0.6	0.6	0.2	2.5	0.3	13.1	13.3	9.3	2.5	2.7	0.7	4.6	4.1				
<b>Non-interest current account deficit</b>	10.8	10.1	11.6	26.8	26.8			34.8	50.8	50.0	44.6	35.9	34.2	29.6	23.1					
Deficit in balance of goods and services	66.8	63.4	58.4	26.0	26.0			23.8	23.4	23.2	23.5	24.1	23.4	20.4	16.6					
Exports	77.6	73.5	70.0	52.8	52.8			58.5	74.1	73.2	68.1	60.0	57.6	50.0	39.7					
Imports	-12.0	-14.6	-11.4	-27.5	-27.5	-9.5	7.7	-35.8	-39.0	-38.0	-36.5	-34.7	-32.6	-27.1	-19.9	-24.9				
Net current transfers (negative = inflow)	0.3	1.2	0.8	1.4	1.4			1.3	1.3	1.3	1.2	1.2	1.2	1.2	1.3					
Other current account flows (negative = net inflow)	-3.0	-2.0	-13.1	-2.4	-2.4	-3.1	3.6	-2.3	-2.2	-2.3	-2.3	-2.2	-2.1	-1.9	-1.5	-1.8				
<b>Net FDI (negative = inflow)</b>	-12.4	-19.8	-18.0	-3.8	-3.8			-0.7	-0.7	-1.6	-2.4	-3.0	-3.0	-1.9	-1.8					
<b>Endogenous debt dynamics 2/</b>	4.5	4.6	2.9	1.9	1.9			2.2	2.1	2.0	1.9	1.6	1.4	0.9	0.4					
Contribution from nominal interest rate	-9.7	-8.3	-6.6	-3.3	-3.3			-2.9	-2.7	-3.6	-4.3	-4.6	-4.4	-2.7	-2.3					
Contribution from real GDP growth	-7.2	-16.1	-14.2	-2.4	-2.4			...	...	...	...	...	...	...	...					
Contribution from price and exchange rate changes	-0.6	2.4	1.9	0.7	0.7			-6.8	-1.7	-0.1	0.3	0.2	-2.1	-1.2	-1.2					
<b>Residual (3-4) 3/</b>	1.9	0.0	-0.6	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0					
o/w exceptional financing	...	...	...	...	...			33.8	40.0	47.2	51.2	49.4	47.0	35.1	23.8					
NPV of external debt 4/	...	...	...	42.7	42.7			142.2	171.3	203.3	218.2	205.0	201.0	172.2	143.6					
In percent of exports	...	...	...	163.9	163.9			23.4	30.9	39.0	43.8	42.7	41.1	31.6	22.6					
<b>NPV of PPG external debt</b>	...	...	...	30.6	30.6			98.7	132.2	167.9	186.7	177.4	175.7	155.1	136.2					
In percent of exports	...	...	...	117.5	117.5			125.1	164.8	204.4	226.8	217.9	209.3	159.0	107.9					
In percent of revenue	...	...	...	158.1	158.1			29.6	14.8	14.3	11.7	10.4	16.6	10.5	6.1					
Debt service-to-exports ratio (in percent)	13.3	11.2	28.1	15.7	15.7			21.7	7.9	8.2	7.3	7.7	9.0	9.1	5.5					
PPG debt service-to-exports ratio (in percent)	10.4	8.2	25.9	12.9	12.9			27.5	9.9	10.0	8.9	9.5	10.8	14.1	11.1					
<b>PPG debt service-to-revenue ratio (in percent)</b>	...	...	...	13.5	13.5			0.1	0.5	0.5	0.4	0.1	0.2	0.3	0.8					
Total gross financing need (billions of U.S. dollars)	0.1	0.0	0.1	0.1	0.1			9.8	4.6	3.9	4.4	5.1	7.2	5.0	4.5					
Non-interest current account deficit that stabilizes debt ratio	16.0	19.4	29.2	5.5	5.5			...	...	...	...	...	...	...	...					
<b>Key macroeconomic assumptions</b>																				
Real GDP growth (in percent)	9.1	10.2	10.6	6.7	6.7	6.1	4.8	7.0	7.5	8.0	8.0	8.0	8.0	7.8	6.5	6.5	6.6			
GDP deflator in US dollar terms (change in percent)	6.2	17.9	20.6	4.5	4.5	10.4	27.6	13.7	3.9	1.9	1.9	1.9	2.9	4.4	2.9	2.9	2.9			
Effective interest rate (percent) 5/	4.2	5.7	4.6	3.7	3.7	4.0	2.0	5.3	5.6	4.5	3.5	2.7	2.6	4.0	2.0	1.2	1.8			
Growth of exports of G&S (US dollar terms, in percent)	8.8	23.2	22.9	-50.3	-50.3	0.0	22.9	11.0	9.9	9.5	11.2	13.0	7.8	10.4	7.0	7.7	7.2			
Growth of imports of G&S (US dollar terms, in percent)	9.7	22.9	27.1	-15.9	-15.9	4.2	14.8	34.8	41.5	8.7	2.3	-2.9	6.5	15.2	6.3	7.4	7.0			
Growth of new public sector borrowing (in percent)	...	...	...	...	...	...	...	29.4	26.1	25.4	26.0	30.1	30.1	27.8	30.1	30.1	30.1			
<i>Memorandum item:</i>																				
Nominal GDP (billions of US dollars)	1.2	1.6	2.1	2.3	2.3			2.8	3.1	3.5	3.8	4.2	4.7	7.5	18.7					

Source: Staff simulations.

1/ Includes both public and private sector external debt.

2/ Derived as  $[r - g - \rho(1+g)] / (1+g-\rho+g)$  times previous period debt ratio, with  $r$  = nominal interest rate;  $g$  = real GDP growth rate, and  $\rho$  = growth rate of GDP deflator in U.S. dollar terms.

3/ Includes exceptional financing (i.e., changes in arrears and debt relief); changes in gross foreign assets; and valuation adjustments. For projections also includes contribution from price and exchange rate changes.

4/ Assumes that NPV of private sector debt is equivalent to its face value.

5/ Current-year interest payments divided by previous period debt stock.

6/ Historical averages and standard deviations are generally derived over the past 10 years, subject to data availability.

Table 2. Tajikistan: External Debt Sustainability Framework, Government Assumes Cotton Sector Debt, 2006-2026 1/

(In percent of GDP, unless otherwise indicated)

	Actual			Historical Average 6/ Standard Deviation 6/	Projections									
	2002	2003	2004		2005	2006	2007	2008	2009	2010	2011	2006-11 Average	2016	2026
<b>External debt (nominal) 1/</b>	106.3	83.5	55.3	50.4	40.9	55.9	64.6	68.9	65.7	61.4	61.4	48.9	38.5	
o/w public and publicly guaranteed (PPG)	78.9	63.7	39.7	37.7	30.6	49.8	59.2	64.0	61.4	57.5	57.5	46.8	37.8	
Change in external debt	-16.9	-22.8	-28.2	-4.8	-9.6	15.0	8.7	4.3	-3.2	-4.4	-4.4	-1.9	0.0	
Identified net debt-creating flows	-16.3	-25.2	-30.1	-5.5	-2.8	10.2	8.6	3.9	-3.4	-2.9	-2.9	-0.3	1.2	
Non-interest current account deficit	-0.9	-3.4	1.0	0.6	0.3	13.1	13.3	9.3	2.5	2.7	2.7	3.7	4.6	4.1
Deficit in balance of goods and services	10.8	10.1	11.6	26.8	34.8	50.8	50.0	44.6	35.9	34.2	34.2	29.6	23.1	
Exports	66.8	63.4	58.4	26.0	23.8	23.4	23.2	23.5	24.1	23.4	23.4	20.4	16.6	
Imports	77.6	73.5	70.0	52.8	58.5	74.1	73.2	68.1	60.0	57.6	57.6	50.0	39.7	
Net current transfers (negative = inflow)	-12.0	-14.6	-11.4	-27.5	-35.8	-39.0	-38.0	-36.5	-34.7	-32.6	-32.6	-27.1	-19.9	-24.9
Other current account flows (negative = net inflow)	0.3	1.2	0.8	1.4	1.3	1.3	1.3	1.2	1.2	1.2	1.2	1.2	1.3	
<b>Net FDI (negative = inflow)</b>	-3.0	-2.0	-13.1	-2.4	-2.3	-2.2	-2.3	-2.3	-2.2	-2.1	-2.1	-1.9	-1.5	-1.8
<b>Endogenous debt dynamics 2/</b>	-12.4	-19.8	-18.0	-3.8	-0.7	-0.7	-2.3	-3.1	-3.6	-3.5	-3.5	-2.2	-1.9	
Contribution from nominal interest rate	4.5	4.6	2.9	1.9	2.2	2.1	1.8	1.6	1.4	1.2	1.2	0.8	0.4	
Contribution from real GDP growth	-9.7	-8.3	-6.6	-3.3	-2.9	-2.7	-4.1	-4.7	-5.0	-4.7	-4.7	-3.0	-2.3	
Contribution from price and exchange rate changes	-7.2	-16.1	-14.2	-2.4	-2.9	-2.7	-4.1	-4.7	-5.0	-4.7	-4.7	-3.0	-2.3	
<b>Residual (3-4) 3/</b>	-0.6	2.4	1.9	0.7	-6.8	4.8	0.1	0.4	0.2	-1.5	-1.5	-1.6	-1.2	
o/w exceptional financing	1.9	0.0	-0.6	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
NPV of external debt 4/	...	...	...	43.3	33.8	44.0	51.0	54.8	52.8	50.9	50.9	38.3	23.5	
In percent of exports	...	...	...	166.3	142.2	188.5	219.6	233.4	219.0	217.6	217.6	187.8	141.9	
<b>NPV of PPG external debt</b>	...	...	...	30.6	23.4	38.0	45.6	49.9	48.4	47.0	47.0	36.1	22.8	
In percent of exports	...	...	...	117.5	98.7	162.5	196.2	212.8	201.0	201.2	201.2	171.1	137.6	
In percent of revenue	...	...	...	158.1	125.1	202.6	238.9	258.5	246.9	239.6	239.6	181.5	109.0	
Debt service-to-exports ratio (in percent)	13.3	11.2	28.1	15.7	29.6	55.7	13.2	10.7	9.6	17.7	17.7	11.7	6.1	
PPG debt service-to-exports ratio (in percent)	10.4	8.2	25.9	12.9	21.7	79.9	9.0	8.0	8.3	9.6	9.6	10.8	5.7	
<b>PPG debt service-to-revenue ratio (in percent)</b>	...	...	...	13.5	27.5	9.9	10.9	9.7	10.2	11.4	11.4	16.2	12.1	
Total gross financing need (billions of U.S. dollars)	0.1	0.0	0.1	0.1	0.1	0.8	0.5	0.4	0.1	0.2	0.2	0.3	0.8	
Non-interest current account deficit that stabilizes debt ratio	16.0	19.4	29.2	5.5	9.8	-1.9	4.5	5.0	5.6	7.1	7.1	5.7	4.6	
<b>Key macroeconomic assumptions</b>														
Real GDP growth (in percent)	9.1	10.2	10.6	6.7	4.8	7.0	7.5	8.0	8.0	8.0	8.0	6.5	6.5	6.6
GDP deflator in US dollar terms (change in percent)	6.2	17.9	20.6	4.5	10.4	13.7	3.9	1.9	1.9	1.9	1.9	2.9	2.9	2.9
Effective interest rate (percent) 5/	4.2	5.7	4.6	3.7	4.0	5.3	5.6	3.4	2.8	2.2	2.1	3.6	1.8	1.1
Growth of exports of G&S (US dollar terms, in percent)	8.8	23.2	22.9	-50.3	0.0	22.9	11.0	9.9	9.5	11.2	13.0	10.4	7.0	7.7
Growth of imports of G&S (US dollar terms, in percent)	9.7	22.9	27.1	-15.9	4.2	14.8	34.8	41.5	8.7	2.3	-2.9	6.5	7.4	7.0
Grant element of new public sector borrowing (in percent)	...	...	...	...	...	...	29.4	26.0	25.4	30.1	30.1	30.1	30.1	30.1
<i>Memorandum item:</i>														
Nominal GDP (billions of US dollars)	1.2	1.6	2.1	2.3	2.8	3.1	3.5	3.8	4.2	4.7	4.7	7.5	18.7	

Source: Staff simulations.

1/ Includes both public and private sector external debt.

2/ Derived as  $(1 - g - \rho(1-g))/(1+g-\rho g)$  times previous period debt ratio, with  $r$  = nominal interest rate;  $g$  = real GDP growth rate, and  $\rho$  = growth rate of GDP deflator in U.S. dollar terms.

3/ Includes exceptional financing (i.e., changes in arrears and debt relief); changes in gross foreign assets; and valuation adjustments. For projections also includes contribution from price and exchange rate changes.

4/ Assumes that NPV of private sector debt is equivalent to its face value.

5/ Current-year interest payments divided by previous period debt stock.

6/ Historical averages and standard deviations are generally derived over the past 10 years, subject to data availability.

Table 3. Tajikistan: External Debt Sustainability Framework, High-Investment Low-Growth Scenario, 2006-2026 1/  
(In percent of GDP, unless otherwise indicated)

	Actual			Historical		Projections										2012-26
	2002	2003	2004	2005	Average 6/ Standard Deviation 6/	2006	2007	2008	2009	2010	2011	2016-11 Average	2016	2026	Average	
<b>External debt (nominal) 1/</b>	106.3	83.5	55.3	50.4		40.9	50.1	60.1	67.5	67.1	64.6	64.6	60.3	69.9		
o/w public and publicly guaranteed (PPG)	78.9	63.7	39.7	38.4		30.6	40.8	51.6	59.6	59.8	57.8	57.8	55.6	67.6		
Change in external debt	-16.9	-22.8	-28.2	-4.8		-9.6	9.2	9.9	7.4	-0.3	-2.6	-2.6	0.2	2.3		
Identified net debt-creating flows	-16.3	-25.2	-30.1	-5.5		-2.8	11.7	11.4	7.1	-0.6	-0.2	-0.2	1.8	4.4		
<b>Non-interest current account deficit</b>	-0.9	-3.4	1.0	0.6	0.2	0.3	13.3	13.6	9.8	2.7	3.1	3.1	5.0	8.4	6.1	
Deficit in balance of goods and services	10.8	10.1	11.6	26.8		34.8	41.5	39.6	36.9	31.9	30.6	30.6	26.6	20.3		
Exports	66.8	63.4	58.4	26.0		23.8	22.6	21.7	21.6	21.7	21.1	21.1	18.3	14.3		
Imports	77.6	73.5	70.0	52.8		58.5	64.2	61.3	58.5	53.6	51.7	51.7	44.9	34.7		
Net current transfers (negative = inflow)	-12.0	-14.6	-11.4	-27.5	7.7	-35.8	-39.5	-38.8	-38.8	-38.2	-37.4	-37.4	-36.4	-36.5		
Other current account flows (negative = net inflow)	0.3	1.2	0.8	1.4		1.3	11.3	12.8	11.7	9.1	9.8	9.8	14.9	24.6		
<b>Net FDI (negative = inflow)</b>	-3.0	-2.0	-13.1	-2.4	3.6	-2.3	-2.3	-2.4	-2.4	-2.5	-2.5	-2.5	-2.5	-2.7		
<b>Endogenous debt dynamics 2/</b>	-12.4	-19.8	-18.0	-3.8		-0.7	0.7	0.2	-0.3	-0.8	-0.9	-0.9	-0.7	-1.3		
Contribution from nominal interest rate	4.5	4.6	2.9	1.9		2.2	2.1	2.1	2.0	1.7	1.6	1.6	1.2	0.8		
Contribution from real GDP growth	-9.7	-8.3	-6.6	-3.3		-2.9	-1.4	-1.8	-2.3	-2.5	-2.5	-2.5	-1.8	-2.1		
Contribution from price and exchange rate changes	-7.2	-16.1	-14.2	-2.4		...	...	...	...	...	...	...	...	...		
<b>Residual (3-4) 3/</b>	-0.6	2.4	1.9	0.7		-6.8	-2.5	-1.5	0.3	0.2	-2.3	-2.3	-1.6	-2.1		
o/w exceptional financing	1.9	0.0	-0.6	0.0		0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		
NPV of external debt 4/	...	...	...	42.7		33.8	40.6	48.3	54.4	54.5	53.8	53.8	47.3	43.7		
In percent of exports	...	...	...	163.9		142.2	179.4	222.5	251.5	250.7	255.1	255.1	257.8	304.5		
<b>NPV of PPG external debt</b>	...	...	...	30.6		23.4	31.3	39.9	46.5	47.1	47.0	47.0	42.6	41.4		
In percent of exports	...	...	...	117.5		98.7	138.4	183.7	215.2	216.9	223.0	223.0	232.2	288.7		
In percent of revenue	...	...	...	158.1		125.1	168.3	202.4	227.0	217.2	209.0	209.0	214.0	198.0		
Debt service-to-exports ratio (in percent)	13.3	11.2	28.1	15.7		29.6	15.5	15.7	13.5	12.7	21.1	21.1	15.8	12.9		
<b>PPG debt service-to-exports ratio (in percent)</b>	10.4	8.2	25.9	12.9		21.7	8.3	9.0	8.5	9.4	11.5	11.5	13.6	11.6		
<b>PPG debt service-to-revenue ratio (in percent)</b>	...	...	...	13.5		27.5	10.1	9.9	8.9	9.4	10.7	10.7	18.9	20.5		
Total gross financing need (billions of U.S. dollars)	0.1	0.0	0.1	0.1		0.1	0.5	0.5	0.4	0.1	0.2	0.2	0.3	0.8		
Non-interest current account deficit that stabilizes debt ratio	16.0	19.4	29.2	5.5		9.8	4.1	3.6	2.4	3.1	5.7	5.7	4.8	6.1		
<b>Key macroeconomic assumptions</b>																
Real GDP growth (in percent)	9.1	10.2	10.6	6.7	6.1	4.8	7.0	3.8	4.0	4.0	4.0	4.0	3.3	3.3	3.3	
GDP deflator in US dollar terms (change in percent)	6.2	17.9	20.6	4.5	10.4	27.6	13.7	6.2	5.0	1.9	2.9	2.9	2.9	2.9	2.9	
Effective interest rate (percent) 5/	4.2	5.7	4.6	3.7	4.0	2.0	5.3	5.6	4.5	3.5	2.7	2.6	4.0	2.0	1.2	
Growth of exports of G&S (US dollar terms, in percent)	8.8	23.2	22.9	-50.3	0.0	22.9	11.0	4.9	4.7	5.6	6.5	3.9	6.1	3.5	3.6	
Growth of imports of G&S (US dollar terms, in percent)	9.7	22.9	27.1	-15.9	4.2	14.8	34.8	20.7	4.4	1.2	-2.9	3.3	10.2	3.1	3.7	
Grant element of new public sector borrowing (in percent)	...	...	...	...	...	...	29.4	26.1	25.4	26.0	30.1	27.8	30.1	30.1	30.1	
<i>Memorandum item:</i>																
Nominal GDP (billions of US dollars)	1.2	1.6	2.1	2.3		2.8	3.1	3.4	3.6	3.8	4.1	4.1	5.5	10.2		

Source: Staff simulations.

1/ Includes both public and private sector external debt.

2/ Derived as  $[(r - g - \rho(1+g)) / (1+g-\rho)]$  times previous period debt ratio, with  $r$  = nominal interest rate;  $g$  = real GDP growth rate, and  $\rho$  = growth rate of GDP deflator in U.S. dollar terms.

3/ Includes exceptional financing (i.e., changes in arrears and debt relief); changes in gross foreign assets, and valuation adjustments. For projections also includes contribution from price and exchange rate changes.

4/ Assumes that NPV of private sector debt is equivalent to its face value.

5/ Current-year interest payments divided by previous period debt stock.

6/ Historical averages and standard deviations are generally derived over the past 10 years, subject to data availability.

Table 4. Tajikistan: Sensitivity Analyses for Key Indicators of Public and Publicly Guaranteed External Debt, 2006-26  
(In percent)

	Projections							
	2006	2007	2008	2009	2010	2011	2016	2026
<b>NPV of debt-to-GDP ratio</b>								
<b>Baseline</b>	23	31	39	44	43	41	32	23
<b>A. Alternative Scenarios</b>								
A1. Key variables at their historical averages in 2007-26 1/	23	21	19	17	14	11	-4	-18
A2. New public sector loans on less favorable terms in 2007-26 2/	23	33	44	50	50	48	41	34
A3. Government assumes cotton sector debt	23	38	46	50	48	47	36	23
A4. High-investment low-growth scenario	23	31	40	47	47	47	43	41
<b>B. Bound Tests</b>								
B1. Real GDP growth at historical average minus one standard deviation in 2007-08	23	31	41	46	45	43	33	24
B2. Export value growth at historical average minus one standard deviation in 2007-08 3/	23	35	50	55	53	51	37	23
B3. US dollar GDP deflator at historical average minus one standard deviation in 2007-08	23	37	54	61	60	57	44	31
B4. Net non-debt creating flows at historical average minus one standard deviation in 2007-08 4/	23	58	92	94	90	85	57	25
B5. Combination of B1-B4 using one-half standard deviation shocks	23	62	107	109	105	100	66	29
B6. One-time 30 percent nominal depreciation relative to the baseline in 2007 5/	23	43	55	62	60	58	44	32
<b>NPV of debt-to-exports ratio</b>								
<b>Baseline</b>	99	132	168	187	177	176	155	136
<b>A. Alternative Scenarios</b>								
A1. Key variables at their historical averages in 2007-26 1/	99	88	80	71	58	47	-22	-108
A2. New public sector loans on less favorable terms in 2007-26 2/	99	143	189	215	206	207	199	205
A3. Government assumes cotton sector debt	99	162	196	213	201	201	177	138
A4. High-investment low-growth scenario	99	138	184	215	217	223	232	289
<b>B. Bound Tests</b>								
B1. Real GDP growth at historical average minus one standard deviation in 2007-08	99	132	168	187	177	176	155	136
B2. Export value growth at historical average minus one standard deviation in 2007-08 3/	99	203	395	423	400	394	331	253
B3. US dollar GDP deflator at historical average minus one standard deviation in 2007-08	99	132	168	187	177	176	155	136
B4. Net non-debt creating flows at historical average minus one standard deviation in 2007-08 4/	99	249	395	399	374	366	279	149
B5. Combination of B1-B4 using one-half standard deviation shocks	99	281	524	531	497	486	372	201
B6. One-time 30 percent nominal depreciation relative to the baseline in 2007 5/	99	132	168	187	177	176	155	136
<b>Debt service ratio</b>								
<b>Baseline</b>	22	8	8	7	8	9	9	5
<b>A. Alternative Scenarios</b>								
A1. Key variables at their historical averages in 2007-26 1/	22	8	7	5	5	6	2	-5
A2. New public sector loans on less favorable terms in 2007-26 2/	22	8	9	9	10	11	16	18
A3. Government assumes cotton sector debt	22	8	9	8	8	10	11	6
A4. High-investment low-growth scenario	22	8	9	8	9	11	14	12
<b>B. Bound Tests</b>								
B1. Real GDP growth at historical average minus one standard deviation in 2007-08	22	8	8	7	8	9	14	14
B2. Export value growth at historical average minus one standard deviation in 2007-08 3/	22	11	16	15	16	18	31	28
B3. US dollar GDP deflator at historical average minus one standard deviation in 2007-08	22	8	8	7	8	9	14	14
B4. Net non-debt creating flows at historical average minus one standard deviation in 2007-08 4/	22	8	11	12	12	13	29	21
B5. Combination of B1-B4 using one-half standard deviation shocks	22	9	14	16	16	18	38	29
B6. One-time 30 percent nominal depreciation relative to the baseline in 2007 5/	22	8	8	7	8	9	14	14
<i>Memorandum item:</i>								
Grant element assumed on residual financing (i.e., financing required above baseline) 6/	29	29	29	29	29	29	29	29

Source: Staff projections and simulations.

1/ Variables include real GDP growth, growth of GDP deflator (in U.S. dollar terms), non-interest current account in percent of GDP, and non-debt creating flows.

2/ Assumes that the interest rate on new borrowing is by 2 percentage points higher than in the baseline, while grace and maturity periods are the same as in the baseline.

3/ Exports values are assumed to remain permanently at the lower level, but the current account as a share of GDP is assumed to return to its baseline level after the shock (implicitly assuming an offsetting adjustment in import levels).

4/ Includes official and private transfers and FDI.

5/ Depreciation is defined as percentage decline in dollar/local currency rate, such that it never exceeds 100 percent.

6/ Applies to all stress scenarios except for A2 (less favorable financing) in which the terms on all new financing are as specified in footnote 2.

Table 4. Tajikistan: Sensitivity Analyses for Key Indicators of Public and Publicly Guaranteed External Debt, 2006-26 (Concluded)  
(In percent)

	Projections							
	2006	2007	2008	2009	2010	2011	2016	2026
<b>NPV of debt-to-revenue ratio</b>								
<b>Baseline</b>	125	165	204	227	218	209	<b>159</b>	108
<b>A. Alternative Scenarios</b>								
A1. Key variables at their historical averages in 2007-26 1/	125	110	97	86	71	56	<b>-22</b>	-85
A2. New public sector loans on less favorable terms in 2007-26 2/	125	178	230	261	253	246	<b>204</b>	162
A3. Government assumes cotton sector debt	125	203	239	259	247	240	<b>182</b>	109
A4. High-investment low-growth scenario	125	168	202	227	217	209	<b>214</b>	198
<b>B. Bound Tests</b>								
B1. Real GDP growth at historical average minus one standard deviation in 2007-08	125	168	213	237	227	218	<b>166</b>	113
B2. Export value growth at historical average minus one standard deviation in 2007-08 3/	125	188	265	283	270	259	<b>187</b>	110
B3. US dollar GDP deflator at historical average minus one standard deviation in 2007-08	125	196	285	316	303	291	<b>221</b>	150
B4. Net non-debt creating flows at historical average minus one standard deviation in 2007-08 4/	125	311	481	485	459	436	<b>286</b>	118
B5. Combination of B1-B4 using one-half standard deviation shocks	125	329	559	565	535	507	<b>334</b>	140
B6. One-time 30 percent nominal depreciation relative to the baseline in 2007 5/	125	232	287	319	306	294	<b>223</b>	152
<b>Debt service-to-revenue</b>								
<b>Baseline</b>	28	10	10	9	9	11	<b>14</b>	11
<b>A. Alternative Scenarios</b>								
A1. Key variables at their historical averages in 2007-26 1/	28	10	9	6	6	7	<b>2</b>	-4
A2. New public sector loans on less favorable terms in 2007-26 2/	28	10	11	11	13	13	<b>16</b>	14
A3. Government assumes cotton sector debt	28	10	11	10	10	11	<b>16</b>	12
A4. High-investment low-growth scenario	28	10	10	9	9	11	<b>19</b>	20
<b>B. Bound Tests</b>								
B1. Real GDP growth at historical average minus one standard deviation in 2007-08	28	10	10	9	10	11	<b>15</b>	12
B2. Export value growth at historical average minus one standard deviation in 2007-08 3/	28	10	11	10	11	12	<b>17</b>	12
B3. US dollar GDP deflator at historical average minus one standard deviation in 2007-08	28	12	14	12	13	15	<b>20</b>	16
B4. Net non-debt creating flows at historical average minus one standard deviation in 2007-08 4/	28	10	13	15	15	16	<b>29</b>	17
B5. Combination of B1-B4 using one-half standard deviation shocks	28	11	15	17	17	18	<b>34</b>	20
B6. One-time 30 percent nominal depreciation relative to the baseline in 2007 5/	28	14	14	13	13	15	<b>20</b>	16

Source: Staff projections and simulations.

1/ Variables include real GDP growth, growth of GDP deflator (in U.S. dollar terms), non-interest current account in percent of GDP, and non-debt creating flows.

2/ Assumes that the interest rate on new borrowing is by 2 percentage points higher than in the baseline, while grace and maturity periods are the same as in the baseline.

3/ Exports values are assumed to remain permanently at the lower level, but the current account as a share of GDP is assumed to return to its baseline level after the shock (implicitly assuming an offsetting adjustment in import levels).

4/ Includes official and private transfers and FDI.

5/ Depreciation is defined as percentage decline in dollar/local currency rate, such that it never exceeds 100 percent.

6/ Applies to all stress scenarios except for A2 (less favorable financing) in which the terms on all new financing are as specified in footnote 2.

INTERNATIONAL MONETARY FUND

REPUBLIC OF TAJIKISTAN

**2006 Article IV Consultation  
Informational Annex**

March 8, 2007

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**ANNEX I:TAJIKISTAN—RELATIONS WITH THE FUND**  
(As of January 31, 2007)

I. **Membership Status:** Joined April 27, 1993; Article VIII

II. **General Resources Account:**

	<u>SDR million</u>	<u>% Quota</u>
Quota	87.00	100.00
Fund holdings of currency	87.00	100.00
Reserve position in Fund	0.00	0.00

III. **SDR Department**

	<u>SDR million</u>	<u>% Allocation</u>
Holdings	2.34	N/A

IV. **Outstanding Purchases and Loans**

	<u>SDR million</u>	<u>% Quota</u>
PRGF arrangements	29.40	33.79

V. **Latest Financial Arrangements**

Type	Approval Date	Expiration Date	Amount Approved (SDR million)	Amount Drawn (SDR million)
PRGF	Dec 11, 2002	Feb 10, 2006	65.00	65.00
ESAF/PRGF	Jun 24, 1998	Dec 24, 2001	100.30	78.28
Stand-by	May 08, 1996	Dec 07, 1996	15.00	15.00

VI. **Projected Payments to Fund**

(SDR million; based on existing use of resources and present holdings of SDRs):

	Forthcoming				
	2007	2008	2009	2010	2011
Principal				0.98	4.90
Charges/Interest	0.15	0.15	0.15	0.15	0.13
Total	0.15	0.15	0.15	1.13	5.03

**VII. Implementation of HIPC Initiative**

Not Applicable.

**VIII. Implementation of MDRI Assistance**

I. Total Debt Relief (SDR Million) 69.31

Of Which MDRI 69.31

HIPC --

II. Debt Relief by Facility (SDR Million)

	<u>Eligible Debt</u>		
<u>Delivery Date</u>	<u>GRA</u>	<u>PRGF</u>	<u>Total</u>
January 2006	N/A	69.31	69.31

**IX. Safeguards Assessment**

The previous safeguards assessment of the NBT was completed on July 23, 2003, which proposed specific measures to address a number of weaknesses, as reported in Country Report No. 03/222. Under the Fund's safeguards assessment policy, while safeguards assessments are optional under the PSI, central banks may undertake such assessments as a way of enhancing their accountability, transparency, and institutional strength, and facilitating quick access to Fund resources in the event of need.

**X. Exchange Rate Arrangements**

The NBT maintains a managed floating exchange rate regime with no preannounced path for the exchange rate. Since August 2005, the NBT has increased the frequency of calculating and announcing the official exchange rate from a weekly to a daily basis. The official exchange rate is based on all interbank transactions in foreign exchange.

With effect from December 9, 2004, the Republic of Tajikistan accepted the obligations of Article VIII, Sections 2, 3, and 4 of the Articles of Agreement. As a result, the Republic of Tajikistan maintains an exchange system that is free of restrictions on the making of payments and transfers for current international transactions, except for exchange restrictions maintained for security reasons that have been notified to the Fund pursuant to Executive Board Decision ([www.imf.org](http://www.imf.org)).

**XI. Article IV Consultation**

The 2004 Article IV consultation was completed on March 18, 2005. Tajikistan is on the 24-month consultation cycle, subject to the provisions of the decision on consultation cycles approved on July 15, 2002.

**XII. Resident Representative**



Mr. Moers, Resident Representative of the Fund, started his assignment in Dushanbe in June 2006.

### XIII. Technical Assistance

The following list summarizes the technical assistance provided by the Fund to Tajikistan since 2002.

#### **Fiscal Affairs:**

July 2004	Revenue Administration Reform
December 2004	Poverty and Social Impact Analysis
June 2005	Public Financial Management
August 2005	Tax Policy and Administration
August 2006	Fiscal ROSC

#### **Monetary and Financial Systems:**

July 2002	Multi-topic
May 2006	Strengthening the Monetary Policy Framework and Liquidity Management

#### **Statistics:**

October/November 2002	Money and Banking Statistics
January 2003	Balance of Payments Statistics
February 2003	Money and Banking Statistics
May 2003	Balance of Payments Statistics
April 2004	Data ROSC
October 2004	General Data Dissemination System (GDDS)
June 2006	Report on Monetary and Financial Statistics

#### **Finance:**

May 2003	Safeguards Assessment Follow-up
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**Legal:**

March 2003

Tax Legislation

January 2004

Tax Legislation

May 2004

Tax Legislation

**ANNEX II:TAJKISTAN—RELATIONS WITH THE WORLD BANK**  
(As of February 15, 2007)

Country Director: Ms. Annette Dixon

Telephone: (202) 473 7089

Country Economist: Mr. Sudharshan Canagarajah

Telephone: (202) 473 4458

**I. Partnership in Tajikistan's Development Strategy**

1. The Bank's Country Partnership Strategy, endorsed by the Bank's Board of Executive Directors on July 26, 2005, focuses on the following three priorities, which are in line with the country's PRSP:

- To improve business opportunities in rural and urban areas
- To enhance and preserve the quality of the human capital
- To improve energy service delivery and increase electricity exports.

2. In addition, in each of the above areas, the Bank Group and government agreed to work to improve government capacity and efficiency, and reduce corruption by giving special emphasis to measures that increase transparency of resource use, reduce discretionary controls, and encourage the participation of users in the provision of services.

3. Macroeconomic management aims at establishing a stable economic environment through appropriate fiscal, monetary, exchange rate, and sustainable debt policies. In support of these policies, the authorities are tightening payment discipline, especially in the energy sector, hardening budget constraints for state-owned enterprises, and pursuing enterprise and banking privatization and restructuring. Recent improvements in macroeconomic management have supported the current economic recovery. However, to maintain strong growth the authorities will need to accelerate structural reform to support private sector development and investment, and encourage foreign investment.

4. The IMF has taken the lead in assisting Tajikistan in enhancing macroeconomic stability. The Fund has encouraged the authorities to continue with fiscal consolidation, maintain a restrictive monetary policy, and conduct prudent debt management policy to enhance its sustainability.

5. The World Bank has taken the lead in the policy dialogue on structural issues, including poverty reduction measures, agriculture sector reforms, private sector development, institution building, budget planning, improving public service delivery, and governance. A range of instruments is used to conduct the dialogue. Policy based lending and technical assistance are supporting reforms in a number of sectors. The Programmatic Development Policy Credit Financing (PDPC)—three year development policy financing program to support government's medium-term reform program—was approved in July 6, 2006; it is supporting the government in the areas of public administration reform, public expenditure management, social service delivery and private sector development.

6. This broad-based approach is combined with sector projects in health, education, municipal infrastructure, power, agriculture, environment, and poverty alleviation. Over the last three years the following studies have been prepared and finalized: the Country Procurement Assessment Review, the Country Financial Accountability Assessment, a Trade Diagnostic Study, an Investment Climate Assessment, Regional Energy Export Potential Study, a Note on Public Sector Wages, the Public Expenditure and Institutional Review, Aviation Sector Note and a Note on development Impact of Remittances. Within Fast Track Initiative (FTI) framework and in anticipation of a sector wide reform currently a Fiduciary Capacity Assessment is being finalized to enable gradual integration and implementation of the donor-funded public investment projects in education. The Bank has recently launched Programmatic Public Expenditure Review and within it a Public Expenditure Tracking Survey in Health and Education, as well as spending efficiency in these two sectors. With support of DFID financing—and technical supervision of the Bank—the Government has adopted a plan to implement Medium-Term Budget Framework which initially will be piloted in Education for the 2008 budget. With Swiss support the Bank has launched the first Public Expenditure and Financial Accountability (PEFA) Assessment in September 2006. The Bank is supporting the development of a Private Sector Development (PSD) Strategy in close coordination with the Government and the Donor Coordination Council in Tajikistan.

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**Tajikistan: Collaboration of the World Bank and the IMF**


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<b>Area</b>	<b>Specialized Advice from Fund</b>	<b>Specialized Advice from Bank</b>	<b>Key Instruments</b>
<b>Economic Framework/ Management</b>	Monetary policy, exchange rate, fiscal, and trade policies, economic statistics	Economic growth, economic statistics	<i>IMF:</i> PRGF performance criteria and benchmarks on monetary and fiscal targets. <i>Bank:</i> First phase of PDPC and Strengthening National Statistics System Project under implementation.
<b>Budget</b>	Medium-term budget framework, tax and customs policy and administration, and treasury and debt management	Budget management, debt management and statistics, public expenditure and financial management reform	<i>IMF:</i> PRGF performance criteria on overall fiscal balance, including PIP. Structural benchmark on treasury development <i>Bank:</i> PDPC, Public Sector Reform Project (PSRP) have been approved; Institutional Development Funds in Public Procurement and External Audit under implementation. Public Finance Management Project (PFMP) under preparation.
<b>Public Sector Reform</b>		Civil service reform, public sector wage reform, public administration reform, health and education financing	<i>IMF:</i> PRGF <i>Bank:</i> PDPC and PSRP under implementation.
<b>Private and Financial Sector Development</b>	Bank supervision; development of the interbank market and increasing competition in the banking sector	Pricing policies, developing and implementing the privatization strategy, farm privatization, cotton debt resolution, land reform	<i>IMF:</i> PRGF conditions on farm privatization, bank closures, and opening the banking sector to foreign competition. <i>Bank:</i> PDPC, Land Cadastre Project under implementation. Cotton Sector Modernization Project under preparation. PSD Strategy Note being finalized.
<b>Other Sectors</b>		Reforms in agriculture, energy sector, water and sanitation, environment, infrastructure.	<i>Bank:</i> PDPC, Municipal Infrastructure Development, Energy Loss Reduction, Dushanbe Water Supply, Land Cadastre, Ferghana Valley Water Projects under implementation. Cotton Sector Modernization Project under preparation.

## II. World Bank Collaboration in Specific Areas

### Areas in which the World Bank leads and there is little direct IMF involvement

7. Areas in which the Bank leads and there is no direct IMF involvement are social sectors, infrastructure and environment. In the social sphere, the Bank has carried out regular *Poverty Assessments* to monitor poverty and develop programs to alleviate poverty. Based on the completed *Living Standards Survey (2003)*, a *Poverty Assessment Update Report* has been prepared. Two *Poverty Alleviation Projects* have supported capacity development at the national and local levels to implement participatory approaches to poverty alleviation and improve the access of the poor to essential economic and social services. In addition, the second *Poverty Alleviation Project* has provided support to vulnerable people through microprojects, microfinance services, and community empowerment. The Bank has been supporting within the framework of the Donor Coordination Council in Tajikistan in the preparation of a new *Poverty Reduction Strategy Paper* for 2007–09, which is expected to be completed soon. Under the *Strengthening National Statistics System Project*, a new Living Standards Survey is being prepared for implementation in 2007.

8. **In education**, the Bank focuses on both addressing policy issues and utilizing IDA credit funds for investments. The ongoing *Education Modernization Project (FY03)* aims to upgrade the basic education system through (a) building capacity for change by providing continued support for strategic changes in curriculum and textbook production and supporting improved management and finance at the national level; and (b) supporting local initiatives for infrastructure and quality improvement, support for textbook rental schemes and book printing, and provision of equipment at the local level. Tajikistan has also received grant funding from the *Education for All (EFA) FTI catalytic fund*, administered by the Bank. Key issues in education, apart from infrastructure rehabilitation and capacity building, are pay reform, per capita financing and expenditure tracking. Assistance to this sector will continue through the *Programmatic Development Policy Financing (PDPF)*, *multi-donor education investment program*, and *PSRP*. Bank's involvement in education also includes wage reform in education and gradual move towards program-based budgeting in the sector through the *PDPF*. The IMF has supported the education reform process, in close collaboration with the World Bank, through a structural benchmark requiring the drawing up of a fully costed education reform plan by the government.

9. **In health**, the Bank is focusing on (a) rationalizing the delivery of the basic health services based on the needs of the population in selected districts, especially in remote areas where the poorest are located; (b) reform the public health services, with particular emphasis on prevention of major communicable diseases such as malaria, tuberculosis and HIV/AIDS; and (c) further strengthening the institutional capability (both at the center and district levels) to carry out health care reforms, to improve the system for budgeting and spending for basic health services, pay reform and to control outbreaks of communicable diseases and prevent HIV/AIDS epidemic from spreading; and (c) implementation of the Basic Benefits Package, wage reform and improving budget allocation mechanism for primary and secondary health care. The *Community and Basic Health Project and PDPF* is main instruments for the implementation of this agenda. Policy dialogue is being carried out under PDPC.

10. With regard to **infrastructure** development, the Bank is concentrating on upgrading basic utility services impacting the population at large and especially the poor. The *Dushanbe Water Supply Project* is helping the Dushanbe Municipality and the local water company to address the most critical deficiencies of water supply services. The *Pamir Private Power Project* is supporting improvements in reliability of electricity supply in the Gorno Badakshan region through private sector participation. The *Energy Loss Reduction Project* is helping to reduce commercial losses and improve the power and gas sector financial viability. *Municipal Infrastructure Project* is providing support to improve urban infrastructure in big towns. The Bank has also been leading policy dialogue (under *PDPF*) on increasing efficiency/viability to ensure long-term growth prospects of the sector.

11. In **agriculture**, the Bank is concentrating on land reform, rehabilitation of irrigation and drainage infrastructure and introduction of market rules in procurement of inputs and marketing of outputs as well as on the resolution of the cotton farm debts. The *Land Registration and Cadastre Project* is assisting the government with the land reform, issuance of land certificates and establishment of a modern cadastre system. The *Ferghana Valley Project* aims to increase water supply and efficiency of irrigation systems in the Ferghana Valley, and develop institutional capacity in land and water resources management. The proposed *Cotton Development Project* (FY07) will help provide alternative financing mechanisms to cotton farmers. Cross cutting policy issues for increasing productivity in cotton sectors are being addressed through the *PDPF*.

12. The Bank has supported programs to improve **environmental management** and to deal with natural disasters. A National Environment Action Plan was developed with the Bank's help. The *Emergency Flood Assistance* and *Lake Sarez Risk Mitigation Projects* have helped the government to mitigate the consequences of frequent natural disasters and to build national capacity to address frequent natural hazards such as mudslides, rock-falls, avalanches, and seasonal floods.

### **Areas in which the World Bank leads and its analysis serves as input into the IMF program**

13. The Bank leads the dialogue on structural reforms through the three year *PDPF* currently under implementation. Institution building and technical assistance in support of *PDPF* structural reforms continue to be provided by the *Education Modernization project*, *Land Registration and Cadastre*, and the *PSRP*. The Bank leads in areas of:

**Private sector development**, including new measures for financial transparency and hard budget constraints, establishment of a new agency to support the private sector and improvements in the regulatory framework, and reduction of taxes on the agricultural sector. The Bank has completed the *Investment Climate Review* and *Agriculture Sector Review* to determine the most important impediments to private sector development. Tajikistan became a part of *Doing Business 2005* which provides insightful and cross-country comparison of business environment in the country. The Bank has been preparing *Private Sector Development Strategy Note* with the Government of Tajikistan.

**Enterprise and farm privatization and reform**, including acceleration of privatization of medium and large enterprises, development of a plan to engage the private sector in Tajikistan's strategic enterprises and adoption of a strategy to privatize these enterprises in a medium term context, improvements to the corporate governance framework public enterprises; upgrading of the status of the Land Reform Committee to the equivalent of a ministry and acceleration of farm privatization and enforcement of procedures to ensure the transparency and equitable privatization of farm land; development of procedures and institutional mechanisms at the state level and selected regions to ensure fair and equitable transfer of land and other farm assets to private individuals or groups; creation of sustainable private family farming units and providing them with the enabling conditions to operate independently in a market economy. The Bank has completed the Investment Climate Review and Agriculture Sector Review to determine the most important impediments to unleashing the agriculture sector potential. With support of donors, the Bank has been providing technical support to the State Property Committee to implement long-term strategic privatization plan; initial actions in restructuring large SOEs has commenced.

**Regulatory reforms**, including focus on (a) changing role of Anti-monopoly Agency and further strengthening its capacity; (b) improving inspection regime for businesses; and (c) easy and transparent rules for business entry (licensing) and exit (bankruptcy regulation). In addition to that, separation of policy making and technical regulators functions in aviation sector is a subject of on-going reforms under *PDPC*. Actions in this area also include initial steps towards separation of airline, airport and air traffic control to improve access to Tajikistan. The discussion on the Review of the Air Transport Sector in Tajikistan has provided the basis for further reforms in this area.

14. While the Bank has taken the lead in privatization and in structural reforms in the private sector as described above, the IMF has also a strong interest in these areas since many of these reforms are critical to achieving macroeconomic stabilization and enhancing growth prospects. Accordingly, there is a high degree of consultation and coordination between the two institutions on these matters.

### **Areas of shared responsibility**

15. The Bank and the Fund are working jointly in the following four main areas (supported by the Bank's PDPF, grants, and several investment operations and the Fund's PRGF):

- **Public sector management.** The Bank has provided technical support to the Government of Tajikistan to develop a comprehensive public administration reform strategy. It includes policy actions in public administration reforms aimed at redefining the role of the state in line with the market economy needs, reorganizing key ministries, strengthening the State Financial Control Committee responsible for budget audits, and supporting the pay reform. The Bank is involved in civil service reform while the Fund is providing technical assistance in support of tax and customs administration and treasury management.



- **Budget planning and execution.** Both institutions work on providing support for a national Treasury, adoption of new Law on Public Finances introducing modern budgetary procedures and improved fiscal management; including Public Investment Program and switching from norm-based costing and allocation of expenditures to activity/population based in education and health sectors. The Bank will continue to provide technical support, and mobilize donor funds, to implement the Medium-Term Budget Framework (MTBF) that was approved by the Government in September 2006. The Bank will also continue to support public financial external and internal control reform through the *PDPC*, *IDFs*, and *PSRP*. Treasury reform will be supported by the forthcoming *PFM* project (FY08).
- **Financial sector reforms.** This area includes the acceleration of financial sector restructuring and closure of weak banks, new regulatory framework for the establishment of non-bank intermediaries; significant changes in the tax code making tax authorities' access to bank accounts conditional on a court authorization. In terms of banking supervision, the IMF is monitoring the closure and merger of banks that do not satisfy prudential requirements. The first FSAP for Tajikistan is being planned in collaboration with the IMF for the first quarter of 2007.
- **Utilities reform.** The Fund has included in the PRGC arrangement conditionality related to energy tariff rates, energy arrears and collection rates with the aim to reduce quasi-fiscal activities and increase transparency. The Bank's program supports this objective, with a focus on enhancing market structures, improved enterprise operation, service delivery, as well as financial performance through *PDPC*. The Bank completed an *Energy Sector Utility Reform Review* in 2004. The Review described the financial condition of the energy sector enterprises and detailed the Bank's medium-term energy sector development strategy. The Bank also approved the *Energy Loss Reduction Project* to help implement the energy sector strategy. It is also working closely together with the Asian Development Bank and the EBRD in the areas of utilities reform and restructuring of strategic enterprises such as the railways and airlines.
- **Debt sustainability analysis:** The Bank and the IMF have started carrying out joint DSAs. The first one was done in early 2006 and a follow up update was completed in February 2007.

### **Areas in which the IMF leads and its analysis serves as input into the World Bank program**

16. The Fund leads the dialogue on fiscal matters, setting the overall envelope for public expenditures. The World Bank's work in key sectors, such as health, education and infrastructure, necessitates close cooperation. In addition to the achievement of overall fiscal targets, the Fund-supported PRGF includes structural benchmarks and performance criteria prohibiting the NBT from issuing directed credit, from making expenditures not related to its core business activities, and from paying dividends while it has negative net worth. This also includes finalization of an inventory of guarantees, pledges, and other contingencies of NBT.

17. In the budgetary area, the Fund is taking the lead on tax reforms and treasury systems development. The IMF also leads the dialogue on policies to rationalize and contain expenditures in the public sector. These include policies regarding wage setting in both the public service, and defining the ceiling for public investment expenditures.

18. In these areas, the Bank takes into account the policy recommendations of the IMF and ensures that its own policy advice is consistent.

### **Areas in which the IMF leads and there is no direct World Bank involvement**

19. The Fund takes the lead in the formulation and execution of fiscal and monetary policies, tax policy, external trade policies, and issues involving economic and financial statistics. However, the World Bank has recently provided an IDA project and catalyzed other donors' financing for the *Strengthening National Statistics System Project*.

### **III. IDA Funding**

20. IDA funding to Tajikistan was provided in the form of 100 percent grant in FY06; FY07 allocation is set with a 45 percent grant component. Tajikistan's eligibility for grants in outer years will be determined based on the annual Debt Sustainability Analyses. The indicative FY06–09 IDA funding is about SDR102 million; the FY06 allocation was SDR 30 million, FY07 allocation is around SDR 26 million.

**ANNEX III: TAJIKISTAN—RELATIONS WITH THE ASIAN DEVELOPMENT BANK**  
(As of February 15, 2007)

Country Director: Mr. Neeraj Jain—Telephone: 992-372-210558/235314/235315

1. Tajikistan became a member of the Asian Development Bank (ADB) in 1998. The ADB has participated in the Consultative Group Meeting for Tajikistan since 1998. After conducting an initial mission in June 1998, ADB completed an Economic Report and Interim Operational Strategy that identified three areas: (a) agriculture; (b) infrastructure rehabilitation (especially energy and transport sectors); and (c) social sector, in which ADB assistance would have the greatest development impact. Based on the Interim Strategy, ADB's Board of Directors approved in October 1998 Tajikistan's country classification, which provides the basis for Tajikistan's full access to concessional resources (Asian Development Fund (ADF)). Based on the new ADF replenishment arrangements completed in 2004, Tajikistan is eligible for receiving 40 percent of the loan amount on grant basis after 2005.
2. In view of Tajikistan's urgent need for assistance in 1998, in coordination with the IMF and the World Bank (WB), the ADB provided a **Post-conflict Infrastructure Program Loan** (\$20 million), which was designed to create a framework for developing market-based transport and energy sectors. The loan was for two years and was fully disbursed by end-2000. Based on the satisfactory progress of the Post-conflict Infrastructure Program loan conditionality, the following loans were approved in these two sectors:
  3. **Transport Sector:** the Road Rehabilitation Project loan (\$20 million in 2000), which rehabilitates the most deteriorated sections of the Dushanbe—Kulyab road in the southern part of Tajikistan, the most civil-war affected areas; and Dushanbe—Kyrgyz Border Road Rehabilitation Project loans (first phase of \$15 million in 2003 and second phase of \$30 million in 2005), which improves Tajikistan's transportation link toward north and east through Kyrgyz Republic, further to Kazakhstan and Russia, as well as to China. These projects also improve rural roads in the project areas. Continued supports in strengthening the government's institutional capacity for efficient management of national road network are provided under technical assistance grants associated with these loans and provided on stand-alone basis.
  4. **Power Sector:** the Power Rehabilitation Project loan (\$34 million in 2000) aims to improve people's quality of life and support poverty reduction by increasing the availability of electricity, and assist in post-conflict recovery of Tajikistan's economy (the project rehabilitates and reinforces power transmission and distribution facilities in the war-damaged areas in Khatlon and Dushanbe regions, and rehabilitates the Nurek Power Plant and Central Hydropower Plant); and the Regional Power Transmission Modernization Project loan (\$20 million in 2002) is geared towards improving the reliability and the operation of the Central Asian power transmission system, enhancing the intercountry power trading between Tajikistan and Uzbekistan, and laying the foundation for a future wholesale regional power market. The later loan had to be cancelled due to the inability of Tajikistan and Uzbekistan agreeing on the Power Trade Agreement. Various technical assistance projects were provided

to accelerate market-oriented reforms in the power sector also in line with IMF and WB programs and for supporting the government in formulating a power sector development strategy. The Tajikistan Afghanistan Power Transmission and Interconnection Project loan is being prepared for ADB Board approval in 2006.

5. In addition to the above, the ADB Board approved to date the following loans to Tajikistan in each sector:

6. **Social Sector:** the Social Sector Rehabilitation Project loan (\$20 million in 1999) to address the serious deterioration in living standards and strengthen the delivery of essential social services; the Health Sector Reform Project loan (\$7.5 million in 2003), which aims to improve health, especially of the poor, women, and children by providing pro-poor health service package, and by reforming the health service delivery and financing mechanism; and the Education Sector Reform Project loan (\$7.5 million in 2003), which focuses on supporting the government's reform priorities in primary (grades 1–4) and general secondary education (grades 5–11) by improving the education system and its management. These two social sector reform loans are being supported by respective grants financed by Japan Fund for Poverty Reduction (JFPR): (a) the project for Community Participation and Public Information Campaign for Health Improvement (\$1 million in 2004); and (b) the School Improvement Project (\$2 million in 2004), which aims to increase access to improved education for children, particularly girls, of poor families and vulnerable groups.

7. **Agriculture Sector:** based on the agriculture sector assessment prepared during 1999–2000, the Agriculture Rehabilitation Project loan (\$35 million in 2002) is being implemented to improve living conditions of the farming communities in the project area and to institute measures to sustain benefits of improvements for irrigation and drainage systems and water supply, as well as by providing farm production support services. In order to support the agriculture sector reforms, the TA for Farm Debt Resolution and Policy Reforms, which is associated with the loan, has been implemented in consultation with the IMF, involving a wide range of stakeholders. Based on the findings of the TA, ADB supported the government in close cooperation with other donors and NGOs for formulating a National Farm Debt Resolution Strategy. A wide range of donor assistance is now needed as the Strategy has been announced by the government. ADB, in collaboration with DFID, is supporting donor coordination for implementing the Strategy. A road map with clearly defined actions, time frame, and results is currently being developed to improve coordination among donors and between donors and the authorities in implementation of the Strategy. Grant assistance for Rural Poverty Reduction Project (\$2.9 million in 2001) financed by JFPR has supported the loan preparation and implementation by pilot testing innovative poverty-oriented on- and off-farm supports. In 2004, Irrigation Rehabilitation Project loan was approved for \$22.7 million. In a major push supporting the agriculture sector and rural development, Sustainable Cotton sub-Sector Project loan and Rural Development Project loan are being prepared for ADB Board approval in 2006.

8. **Finance:** Microfinance Systems Development Program loan (\$4 million in 2003) to support policy, legal, and regulatory reforms; and Microfinance Systems Development

Project loan (\$4 million in 2003) to help transform nongovernmental organization microfinance programs into licensed and regulated microfinance institutions.

9. **Trade Facilitation:** the Regional Trade Facilitation and Customs Cooperation Program loan (\$10 million in 2002), which supports trade and customs reform development across the East and Central Asia. Regional Customs Modernization and Infrastructure Development (\$10.7 million in 2004) to promote international trade and enabling environment for private sector development.

10. **Emergency Assistance:** in response to the government's urgent requests, three emergency loans, including the Emergency Flood Rehabilitation Project loan (\$5 million in 1999), the Emergency Restoration of Yavan Water Conveyance System loan (\$3.6 million in 2001), and the Emergency Baipaza Landslide Stabilization Project loan (\$5.3 million in 2002) were approved.

11. As of August 2006, in addition to the above 18 loans, totaling \$264.4 million, and 6 JFPR grant projects, totaling \$10.2 million, ADB provided 46 technical assistance grants, totaling \$23.1 million to support policy reforms, capacity building, and project implementation.

12. In end-2000, ADB started supporting the government in developing PRSP through participatory approach under a TA grant in close cooperation with the IMF, WB, and UNDP. Following the finalization of the PRSP in June 2002, ADB concluded the Poverty Partnership Agreement (PPA) with the government in December 2002, and proceeded to prepare a new five-year Country Strategy and Program (CSP) for 2004–08 for Tajikistan, which was endorsed by the ADB Board in October 2003. Its main objectives are (a) to strengthen rural development through institution building that will support policy implementation and the private sector; (b) to rehabilitate power and rural infrastructure; and (c) to strengthen regional cooperation through improved customs services and transport links, both within the country and neighboring ones.

13. ADB prepares and updates its three-year rolling programs for Tajikistan every year in consultation with the government based on the ADF resources availability, carefully examining the country's social and economic development status and in coordination with other donors, including IMF. The Country Strategy Update for 2006–08 was approved by the Board in August 2005. The Update for 2007–2009 is currently under preparation. ADB pays full attention to the progress of Tajikistan's MDG achievement. ADB is paying intensive attention to governance reforms through investment projects and technical assistance. In 2006, ADB is leading a multi-donor consortium for a technical assistance project entitled Strengthening Results Management in Support of Poverty Reduction in Tajikistan. In 2007, ADB would launch significant technical assistance for implementation of the Private Sector Development Strategy for Tajikistan. ADB is also currently preparing Tax Administration Modernization and Governance Enhancement Project loan for ADB Board approval in 2007.

The total country indicative planning figure of ADF lending level for Tajikistan is \$88.5 million including \$31.0 million in grants for 2007–09 including. Moreover, Tajikistan

will be a potential candidate for regional projects amounting to \$85 million over 2007–09. In addition, nonlending operations are proposed for \$4.9 million over 2007–08. These exclude cofinancing. The actual lending level will be determined by (a) availability of overall ADF resources; (b) country performance assessment vis-à-vis ADB's policy on performance based allocation of ADF resources; and (c) processing status of the projects in the pipeline.

#### ANNEX IV: TAJIKISTAN—STATISTICAL ISSUES

1. Data provision is broadly adequate for surveillance purposes. Tajikistan began participation in the GDDS in November 2004 and the country page in the *International Financial Statistics (IFS)* has been published since February 2003.
2. The authorities have indicated their interest in subscribing to the Fund's SDDS. They have appointed a national SDDS coordinator and requested technical assistance for this purpose. Before subscribing to the SDDS, Tajikistan will need to compile and disseminate the following datasets: quarterly national accounts, template on international reserves and foreign currency liquidity, and international investment position. Also, Tajikistan will need to disseminate regularly general government operations that include special funds (extra-budgetary accounts) at least on an annual basis, quarterly central government debt, monthly gross international reserves, and quarterly external debt data, with improved timeliness for several data categories.
3. The data ROSC mission in April 2004 found that the consumer price index, government finance statistics (GFS), and monetary statistics broadly follow sound methodologies. The mission also noted that source data are well-developed in all areas of statistics, and that suitable processes for assessment and validation of source data are in place. However, further efforts to improve the quality of economic statistics are limited by tight budgetary constraints.

#### **National Accounts and Price Statistics**

4. The ROSC mission identified significant deficiencies in statistical techniques for national accounts and price statistics, most notably in procedures to estimate the informal economy, and in the techniques for imputation, replacement, quality adjustment, and introduction of new products in the price indices. In addition, an intensified effort is needed to strengthen the scope, classification/sectorization, and basis of recording of the national accounts, and to reconsider the concepts and basis of recording underlying the producer price index (PPI).

#### **Fiscal Statistics**

5. The government finance statistics are based on cash transactions as recommended in *A Manual on Government Finance Statistics, 1986*. Although there are no plans at present to migrate the basis of compilation to the *Government Finance Statistics Manual 2001*, the cash GFS operations data were reported in the new framework for inclusion in the *2005 GFS Yearbook*, although no details on financing of the cash deficit were reported. Data with a higher frequency for inclusion in the IFS are not reported.

**Monetary and Financial Statistics**

6. A monetary and financial statistics mission visited Tajikistan in early 2006 and assisted the authorities in establishing the procedures for compiling analytical accounts for commercial banks using data collected from the revised chart of accounts. The mission also assisted the authorities in implementing the Standardized Report Forms (SRFs) developed by STA. The authorities resumed regular reporting of monthly monetary data to STA for publication in IFS shortly after the mission. Further efforts are needed to implement the SRFs and the mission's other recommendations for improving the collection, compilation, and dissemination.

**Balance of Payments Statistics**

7. There is a need for consistency in applying the residency concept in the balance of payments and the national accounts, and the scope of the foreign trade data needs to be improved to cover the shuttle trade.



**TAJKISTAN: TABLE OF COMMON INDICATORS REQUIRED FOR SURVEILLANCE**  
(As of February 23, 2007)

	Date of latest observation	Date received	Frequency of Data <sup>6</sup>	Frequency of Reporting <sup>6</sup>	Frequency of publication <sup>6</sup>	Memo Items:	
						Data Quality – Methodological soundness <sup>7</sup>	Data Quality – Accuracy and reliability <sup>8</sup>
Exchange Rates	2/9/07	2/16/07	D	W	W		
International Reserve Assets and Reserve Liabilities of the Monetary Authorities <sup>1</sup>	1/31/07	2/8/07	W	W	W		
Reserve/Base Money	12/31/06	2/6/07	W	W	W	O, O, LO O	LO, O, O, O, NO
Broad Money	12/31/06	2/6/07	M	M	M		
Central Bank Balance Sheet	12/31/06	2/6/07	W	W	W		
Consolidated Balance Sheet of the Banking System	12/31/06	2/6/07	M	M	M		
Interest Rates <sup>2</sup>	1/31/07	2/6/07	W	W	V		
Consumer Price Index	1/31/07	2/19/07	M	M	M	LO, LO, LNO, O	LO, LO, LO, O, O
Revenue, Expenditure, Balance and Composition of Financing <sup>3</sup> — General Government <sup>4</sup>	12/31/06	1/31/07	M	M	M	LO, LO, O, O	O, O, O, LO, LO
Revenue, Expenditure, Balance and Composition of Financing <sup>3</sup> — Central Government	12/31/06	1/31/07	M	M	M		
Stocks of Central Government and Central Government-Guaranteed Debt	Q4/06	2/2/07	Q	Q	V		
External Current Account Balance	Q4/06	2/2/07	Q	Q	V	LNO, LNO, O, O	LO, O, O, O, O
Exports and Imports of Goods and Services	Q4/06	2/2/07	Q	Q	V		
GDP/GNP	1/31/07	2/19/07	M	M	V	O, LNO, LNO, LNO	LO, LO, LNO, O, O
Gross External Debt <sup>5</sup>	12/31/07	2/2/07	Q	Q	V		

<sup>1</sup>Includes reserve assets pledged or otherwise encumbered, as well as net derivative positions.

<sup>2</sup>Both market-based and officially determined, including discount rates, money market rates, and rates on treasury bills, notes and bonds.

<sup>3</sup>Foreign, domestic bank, and domestic nonbank financing.

<sup>4</sup>The general government comprises central government (budgetary, extra budgetary, and social protection funds) and state and local governments.

<sup>5</sup>Including currency and maturity composition.

<sup>6</sup>Daily (D), Weekly (W), Monthly (M), Quarterly (Q), Annually (A); NA: Not Available.

<sup>7</sup>Reflects the assessment provided in the data ROSC published in April 2005 and based on the findings of the staff mission during April 2004 for the dataset corresponding to the variable in each row. The assessment indicates whether international standards concerning concepts and definitions, scope, classification/sectorization, and basis for recording are fully observed (O), largely observed (LO), largely not observed (LNO), or not observed (NO).

<sup>8</sup>Same as footnote 8, except referring to international standards concerning source data, statistical techniques, assessment and validation of source data, assessment and validation of intermediate data and statistical outputs, and revision studies.



INTERNATIONAL MONETARY FUND

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FOR IMMEDIATE RELEASE  
April 10, 2007

International Monetary Fund  
700 19<sup>th</sup> Street, NW  
Washington, D. C. 20431 USA

## **IMF Executive Board Concludes 2006 Article IV Consultation with the Republic of Tajikistan**

On March 28, 2007, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation with the Republic of Tajikistan.<sup>1</sup>

### **Background**

While the recent strong growth performance continued in 2006, inflation accelerated. Despite considerable disruptions to energy supply late in the year, real GDP growth reached 7 percent, fueled by a surge in construction activity and continuing strong remittance-financed demand for retail services. However, CPI-inflation reached 12.7 percent, its highest level since 2003, mostly because of failed harvests and higher gas prices, but also reflecting a relatively passive monetary policy stance. High aluminum prices and strong growth in nontraditional exports and workers' remittances did not translate into a commensurate improvement in the external accounts, as higher energy prices and strong demand for consumer and capital goods led to a surge in imports. Gross reserves remain relatively low, at the equivalent of two months of imports.

Fiscal policy remained prudent. Reflecting strong revenue performance and cautious fiscal management, the 2006 budget recorded a surplus, continuing the impressive fiscal performance of the past four years. While Tajikistan's external debt profile has improved significantly—mostly as a result of debt restructuring operations and relief under the Multilateral Debt Relief Initiative

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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.

—on current trends, total public and publicly guaranteed debt is projected to increase significantly over the period of 2006–2009, mainly because of large project-related disbursements from China.

Progress in the structural reform area has been mixed. The authorities have been successfully implementing tax administration and public financial management reforms. While further headway has been made in strengthening the banking sector, it remains small and vulnerable, and public disclosure requirements continue to be inadequate. In the energy sector, important steps have been taken to align tariffs with costs; however, structural and regulatory weaknesses continue to undermine its potential. Agricultural reforms are on going, although finding a solution to the debt overhang in the cotton sector is still an outstanding policy issue. Enhancing growth prospects will also require improving the private investment climate. In this vein, the forthcoming second Poverty Reduction Strategy Paper is expected to address some of these issues.

### **Executive Board Assessment**

Executive Directors commended the authorities for their progress in stabilizing the economy and their implementation of sound economic policies and structural reforms that have contributed to high rates of economic growth. Together with debt relief and macroeconomic stability, strong growth has led to significant progress toward meeting the Millennium Development Goals, including poverty reduction. At the same time, Directors observed that major challenges remain. Inflation pressures have resurfaced, debt sustainability could become a concern with rising indebtedness, and poverty remains widespread.

Directors commended the authorities for their strong fiscal performance in 2006. They urged the authorities to continue to implement a sound fiscal policy in 2007 and save any revenue overperformance, particularly since inflation is on an upward trend and the debt dynamics are worsening. Directors encouraged the authorities to refrain from adopting a supplementary budget until the inflation picture improves. Directors welcomed the significant progress achieved in the areas of tax administration, civil service reform, and public financial management. Nevertheless, the authorities need to address urgently remaining weaknesses in tax compliance and the financial monitoring of state enterprises.

Directors underscored the importance of controlling inflation. The macroeconomic policy framework should be buttressed not only by a strong fiscal position and a flexible exchange rate, but also by a tighter monetary stance. In this context, the balance sheet of the central bank needs to be placed on a firmer footing to give more flexibility and credibility to monetary policy. Directors advised the central bank to refrain from providing directed credits to the agricultural sector. Any financial resources directed to the private sector, particularly if subsidized, should be channeled through the budget in a transparent manner.

Directors supported the current managed float exchange rate regime, which they considered has served Tajikistan well. They encouraged the authorities to limit intervention in the foreign exchange market to smoothing operations and shoring up reserve coverage.

Directors observed that the authorities' development strategy, centered on financing essential infrastructure investments through large and rapidly disbursing project loans at concessional interest rates, could entail risks to debt sustainability in the longer term if the expected concomitant acceleration in growth does not materialize. In addition, many Directors cautioned that the rapid debt accumulation could place additional pressure on the budget, as significant counterpart funds would be needed, which could reduce resources available for other priority sectors and affect macroeconomic performance. Against that background, Directors welcomed the authorities' intention to put in place a debt management strategy that will prevent public debt from exceeding 60 percent of GDP.

Directors considered that the authorities' medium-term growth objectives are ambitious but achievable. Reaching these goals will require determination on the part of the government to address long-standing policy issues in the agricultural and energy sectors, intensify efforts to improve the private investment climate, promote the channeling of the large volume of private remittances to the most productive uses, and enhance the governance framework for state-owned enterprises. Directors welcomed the authorities' intention to focus the second poverty reduction strategy paper on efforts to improve the private investment climate and move forward with the public sector reform program.

Directors welcomed the authorities' commitment to continue with the reforms of core macroeconomic institutions. They looked forward to even closer cooperation and discussion between the authorities and the staff in the period ahead, with a view to the design of a program that could elicit Fund support.

**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

	2003	2004	2005	2006 (prel.)
	(Annual percent change)			
Production and prices				
Real GDP	10.2	10.6	6.7	7.0
CPI (e.o.p.)	13.7	5.7	7.1	12.7
General government				
Total revenues and grants	17.3	17.9	20.1	23.4
Total expenditure	19.1	20.3	23.0	21.7
Balance (incl. PIP)	-1.8	-2.4	-2.9	1.7
Balance (excl. PIP & MDRI)	0.9	0.7	0.5	0.8
Monetary indicators				
Broad money	28.6	14.1	23.9	40.6
Velocity of broad money 1/	3.0	3.7	3.5	3.3
External sector 2/				
Exports of goods & services	985	1,211	601	668
Imports of goods & services	1,142	1,451	1,221	1,646
Current account balance	-20	-82	-58	-70
In percent of GDP	-1.3	-3.9	-2.5	-2.5
Gross international reserves	135	189	224	252
In months of imports 3/	1.8	2.5	2.1	2.0

Sources: Tajik authorities; and IMF staff estimates.

1/ Four-quarter average.

2/ Starting from 2005, export and import figures reflect the transition to tolling arrangement for aluminum exports. Therefore, they show a sudden drop compared to earlier years.

3/ Excluding electricity, which trades on a barter basis, and imports related to projects financed by loans from China.

**Statement by Thomas Moser, Executive Director for Republic of Tajikistan**  
**March 28, 2007**

1. My Tajik authorities would like to thank staff for the very constructive policy dialogue. They highly appreciate the support from the Fund. As the staff report notes, Tajikistan's performance under two previous arrangements (1998-2005) was strong, and last year's Ex Post Assessment concluded that "Tajikistan's engagement with the Fund is on balance a success story." The authorities fully share this view, and they would very much appreciate a new Fund arrangement, which could play a critical role in helping to safeguard macroeconomic stability and tackle the outstanding structural reform agenda.

**Recent Developments and Economic Policies**

2. Real GDP growth has again been strong in 2006, supported by all sectors. The main drivers, however, were the construction sector and remittances, which financed demand for services. The surge in construction activity and the spike in energy prices further complicated monetary policy, which already has to manage the substantial remittances inflows. The authorities' decision to pass through fully the cost of significantly higher gas prices and higher food prices due to the failed harvest have contributed to the increase in inflation.

3. While inflation is expected to recede partly, absent negative exogenous shocks, the authorities' objective of 7 percent inflation for 2007 will be difficult to achieve. The National Bank of Tajikistan (NBT) is therefore considering aiming for a more credible inflation target in the range of 8-9 percent. The authorities remain committed to a flexible exchange rate regime and intend to limit foreign exchange interventions to smoothing exchange rate movements. To strengthen the monetary policy framework, efforts are underway to widen the menu of monetary policy instruments available to the NBT. A working group has recently been established to develop the next steps. The authorities are also looking forward to the FSAP mission and its recommendations, which will be useful for moving forward with the restoration of the capital position of the NBT.

4. A strong fiscal policy stance continued to be the centerpiece of macroeconomic policy. As noted in the staff report, the 2006 budget recorded a better-than-expected surplus, despite the election cycle, with tax revenues over-performing. It should be pointed out that Tajikistan has achieved a remarkably successful fiscal consolidation under Fund-supported programs. The overall fiscal balance, excluding the externally financed Public Investment Program, turned from a deficit of about 4 percent of GDP in 1998 to surplus since 2002, while at the same time the authorities have made good progress in reprioritizing expenditures towards social sectors. Significant progress has also been achieved in tax administration and public financial management, as highlighted in Boxes 3 and 4 of the staff report.

5. The staff report rightly points out, however, that the implementation of some key structural reforms is still pending, particularly in the agricultural and energy sectors. The authorities share the staff's view that the cotton debt problem in the agricultural sector must be resolved. To make progress, they have endorsed on March 5, 2007, a "Road Map" attached to the existing cotton debt strategy approved last year. The "Road Map" envisages, among others, to eliminate interference and implicit governance of the local governments on cotton harvesting. These efforts should help address the remaining distortions that exist despite the crucial progress made on land reform. Given the complexity of the cotton debt problem, the authorities continue to seek technical assistance.

6. The Poverty Reduction Strategy Paper (PRSP) II draft was distributed to the donor's community. The main objective of PRSP II is to concentrate on improving the investment climate, make progress with the public sector reforms, while sustaining macroeconomic stability and reducing further poverty. The PRSP II draft will be discussed at the technical level among donors at a meeting to be held in Switzerland in April.

### **The Development Strategy and the Debt Issue**

7. As pointed out in the staff report, Tajikistan has significant development potential, particularly in the agricultural and electricity sector. Currently, however, inadequate energy infrastructure causes severe electricity shortages, characterized by regular electricity blackouts and many areas having only two hours of electricity per day during winter months. In order to improve the quantity and reliability of electricity supply, the authorities have arranged for concessional loans to construct two large electricity transmission lines and new hydroelectricity projects. The authorities would like to point out, as the G-8 did at its 2006 Summit in St. Petersburg, that it is impossible to drastically reduce poverty, support health services, provide clean drinking water and sanitation, promote more productive agriculture, and secure investment in job-creating enterprises without addressing the serious energy problems. The authorities have further signed a concessional loan for a road project linking Tajikistan and Uzbekistan, which would substantially reduce traveling distance and help promote regional economic integration.

8. These concessional loans amount to USD 1 billion and bring the debt-to-GDP ratio to a projected 56 percent by end-2009. The authorities believe that the projects that are financed with these loans will improve Tajikistan's growth potential and debt capacity. As pointed out in the staff report, the World Bank agrees that these projects have the potential to contribute to Tajikistan's long-term growth prospects. Moreover, in recognition of significant advances in macroeconomic management and governance, the World Bank has recently reclassified Tajikistan as a "medium-performer," which also implies a higher debt capacity.

9. However, the authorities understand that their borrowing strategy raises concerns about debt sustainability, particularly the pace of debt accumulation. To address these

concerns, they intend to adopt a well-defined debt management strategy, the key pillars of which would be (1) a zero ceiling on contracting non-concessional debt, and (2) a medium-term foreign debt ceiling of 60 percent of GDP. The joint Fund-Bank external debt sustainability analysis shows that under the baseline scenario, Tajikistan's debt would remain sustainable and debt service payments manageable. Under the historical scenario, all debt burden ratios not only remain well below the threshold indicators but also follow a downward trend throughout the projection period. It should also be recalled that fiscal prudence and adherence to fiscal targets have been a strength under previous Fund programs, which helped the authorities to reduce the external debt-to-GDP ratio from about 130 percent at the end of the 1990s to about 50 percent in 2005 before receiving MDRI relief.

### **Which Reforms Could a New Fund Arrangement Support?**

10. In addition to the debt management strategy outlined above, the authorities intend to make further improvements in tax and customs administration, and they are aware of the need to address the high level of tax arrears. They are also committed to improve public expenditure policy and management, including the financial monitoring of state enterprises. A new Fund arrangement could help to gather internal support for such measures, including for the above mentioned borrowing ceilings.

11. The authorities aim to strengthen monetary policy management and develop the banking sector. A new Fund arrangement could help the authorities to design the appropriate policy framework and the results of the forthcoming FSAP could be incorporated.

12. The authorities will work closely with the World Bank on energy sector reform, including a plan to improve energy sector finances. On February 1, the authorities increased electricity tariffs by 25 percent. The authorities intend to make further progress toward cost-recovery, accompanied by improvements in the social assistance mechanism. With the assistance of the World Bank and the Asian Development Bank, they also intend to continue with reforms of the agricultural, civil service, and education sectors.