



## TURKMENISTAN

### Highlights

- **Officially reported GDP shows strong growth figures.** Growth of GDP remains above 6 per cent, driven by an acceleration of growth in industry. The official exchange rate remains overvalued at 3.5 manats per US dollar but pressures on the parallel market exchange rate have been easing since the beginning of 2019.
- **Turkmenistan has signed a long-awaited five-year contract with Russia for gas delivery.** Regular gas supplies to Russia had been stopped since 2016. The new contract reduces Turkmenistan's dependence on China as its sole gas export market.
- **Free access to electricity, gas and water ended in 2019.** This is indicative of the government's stated intention to move to a market-based economy and improve public finances.

### Key priorities for 2020

- **Currency convertibility issues need to be addressed and the exchange rate should be adjusted to reflect macroeconomic fundamentals.** Removing exchange rate distortions would improve the competitiveness of the country's exports and correct external imbalances while stimulating growth of the private sector.
- **The authorities need to reduce the role of the state in the distribution of resources.** Key necessary steps include the commercialisation of state-owned enterprises, transparent privatisation, and a reduction in state-directed lending.
- **It is critical to deal with governance gaps.** Greater transparency and data availability, stronger protection of property rights, and an improved regulatory environment are essential for enabling foreign direct investment (FDI) inflows and strengthening the role of the private sector.

#### Main macroeconomic indicators %

	2015	2016	2017	2018	2019 proj.
GDP growth	6.5	6.2	6.5	6.2	6.3
Inflation (average)	7.4	3.6	8.0	13.2	13.5
Government balance/GDP	-0.7	-2.4	-2.8	-0.2	-0.1
Current account balance/GDP	-15.6	-20.2	-10.3	5.7	-1.0
Net FDI/GDP [neg. sign = inflows]	-8.5	-6.2	-5.5	-4.9	-5.0
External debt/GDP	21.8	23.1	25.1	25.4	n.a.
Gross reserves/GDP	n.a.	n.a.	n.a.	n.a.	n.a.
Credit to private sector/GDP	n.a.	n.a.	n.a.	n.a.	n.a.

### Macroeconomic performance

**The economy continues to grow strongly according to official figures.** Reliable economic data are hard to find in Turkmenistan but, according to official figures, economic growth remains above 6 per cent. The growth rate accelerated marginally to 6.3 per cent year-on-year in the first three quarters of 2019 from 6.2 per cent in 2018. This was enabled by acceleration of growth in industry (6.9 per cent versus 4.6 per cent a year earlier). Exports were reported to have risen by 7.5 per cent year-on-year in the first three quarters of 2019, helped by a resumption of gas exports to Russia. Imports contracted by 5 per cent in the same period. Retail trade turnover increased by 19 per cent in the period January to July 2019. Credit growth reached around 10 per cent in the first half of 2019. However, fixed investment continued to contract as public spending decreased.

**The exchange rate remains overvalued and exchange rate controls continue to be imposed.**

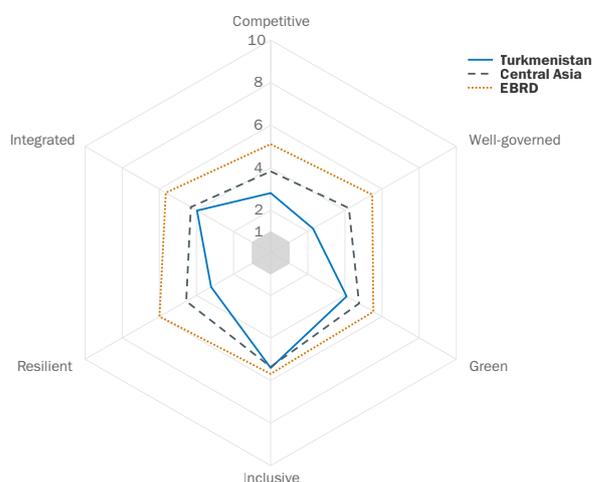
The central bank is still implementing foreign exchange rationing, which severely disrupts foreign trade and profit repatriation. While exports recovered to US\$ 11.2 billion (26 per cent of GDP) in 2018 after a deep slump in the previous two years, it remains uncertain how much of the exports actually translate to export proceeds. The gap between the official and unofficial exchange rates has widened significantly, suggesting that the manat is overvalued. The parallel market exchange rate stayed around 17 to 19 manats per US dollar in the first three quarters of 2019 (well above the official rate of 3.5 manats), but pressures have been easing since the beginning of the year. Average inflation accelerated to 13.6 per cent in 2018 from 8.0 per cent in 2017, also due to increases in public sector wages and pensions and higher gasoline prices.

**Fiscal adjustment is proceeding and the external position has improved.**

The general government fiscal balance turned to a surplus of 0.6 per cent of GDP in 2018 from a deficit of 2.8 per cent in the previous year. This was enabled by reductions in state subsidies and cuts in capital expenditure. The current account registered a surplus of 3.1 per cent of GDP in 2018 (versus a deficit of 10.3 per cent in 2017). Higher gas demand from China enabled strong export growth in 2018 (by 49.6 per cent year-on-year in US dollar terms). In contrast, registered imports declined by 47.8 per cent in 2018.

**GDP growth is forecast to moderate slightly in the short term.** We expect GDP to grow by 6.3 per cent in 2018 and 6.0 per cent in 2019, provided the external demand for gas remains favourable, although we note the difficulty of providing forecasts in the absence of reliable data. The resumption of gas exports to Russia following a three-year interruption is expected to improve growth prospects. Growth will continue to be weighed down by fiscal restraint, restricted access to foreign exchange except for priority projects, a difficult business environment and limited FDI inflows.

#### Assessment of transition qualities (1-10)



## Major structural reform developments

**The government has ended social transfers for electricity, gas and water.** The relevant decree was signed in September 2018 and took effect from January 2019. Turkmen citizens had enjoyed such benefits since late 1992. This termination of transfers is an indication of the government's stated intention to move to a market-based economy but is also suggestive of the difficult economic conditions faced by the country, notwithstanding the reported high growth rates. In addition, the government intends to increase domestic gasoline prices, which are currently among the lowest in the region, to achieve cost-recovery levels. The most recent price hike (by about 50 per cent) was implemented in February 2018.

**Turkmenistan has signed a long-awaited five-year contract with Gazprom.** Under the terms of the contract, signed in July 2019, 5.5 billion cubic metres (bcm) of gas will be exported to Russia annually. This follows the short contract signed in mid-April 2019 for delivery of 1.2 bcm of Turkmen gas from April to June 2019 (Russia had stopped buying Turkmen gas at the beginning of 2016). There are no details on pricing. The new contract is likely to somewhat ease the pressure on the external accounts and reduce the country's dependence on China as its sole gas export market.

**Turkmenistan has ratified the convention on the legal status of the Caspian Sea.** Ratification took place in December 2018 and follows signing of the convention by Azerbaijan, Iran, Kazakhstan, Russia and Turkmenistan in August 2018. This is an important milestone for the region after more than 20 years of discussions, and it ends the dispute over ownership of water resources. The Caspian Sea has been granted a special legal status, whereby each of the five countries has 15 miles from the coast of territorial waters and a further 10 miles of sovereign fishing waters. The convention makes it possible to build pipelines along the seabed, provided they adhere to environmental requirements. It therefore lays the foundation for construction of the Trans-Caspian pipeline between Turkmenistan and Azerbaijan, which would deliver gas from Turkmenistan to Turkey and then to Europe. Further uncertainties remain regarding the delimitation of the seabed and subsoil resources, but nevertheless the agreement represents an important step for major energy projects.

**A land fund established in October 2018 will allocate land to private farmers under a lease of up to 99 years.** The land transferred to tenants for long-term use should be used only for agricultural purposes. Farmers are required to use 70 per cent of the land to grow crops (cotton and wheat) to fulfil government demand. In addition, state purchasing prices for those crops have been increased since January 2019. The government also subsidises farming costs by providing concessional loans, at 1 per cent interest for 10 years, to finance acquisition of agricultural equipment. These measures are designed to promote the growth of agriculture and to increase productivity of the sector.

**Foreign investors have filed several cases against the government of Turkmenistan.** In April 2019 MTS, a Russian telecommunications company, filed a case against Turkmenistan with the International Centre for Settlement of Investment Disputes (ICSID), an international arbitration institution. MTS states that it had to terminate its operations in Turkmenistan because of the government's actions, with losses amounting to US\$ 1.5 billion. In October 2018 SECE Group, a Turkish construction company, and Unionmatex, a German engineering company, also filed cases with ICSID, citing the non-payments of contractually owed monies by the Turkmen government. These add to a few other arbitration cases pending since 2009. Weak property rights and a complex regulatory environment characterised by arbitrary enforcement continue to constrain the inflow of FDI and are major obstacles to doing business in the country.