

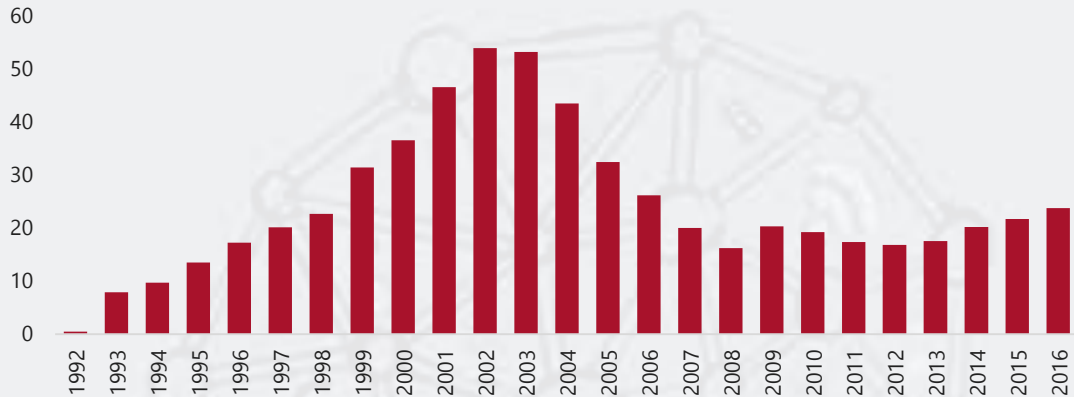
The background of the slide is a photograph of an open book. The pages are filled with text and diagrams. A pair of gold-rimmed glasses is placed on the left page. The right page features a tree diagram with several levels of nodes. The overall image is slightly blurred and has a soft, warm light.

THE CONTEXT OF ECONOMIC REFORMS IN UZBEKISTAN

June 2018

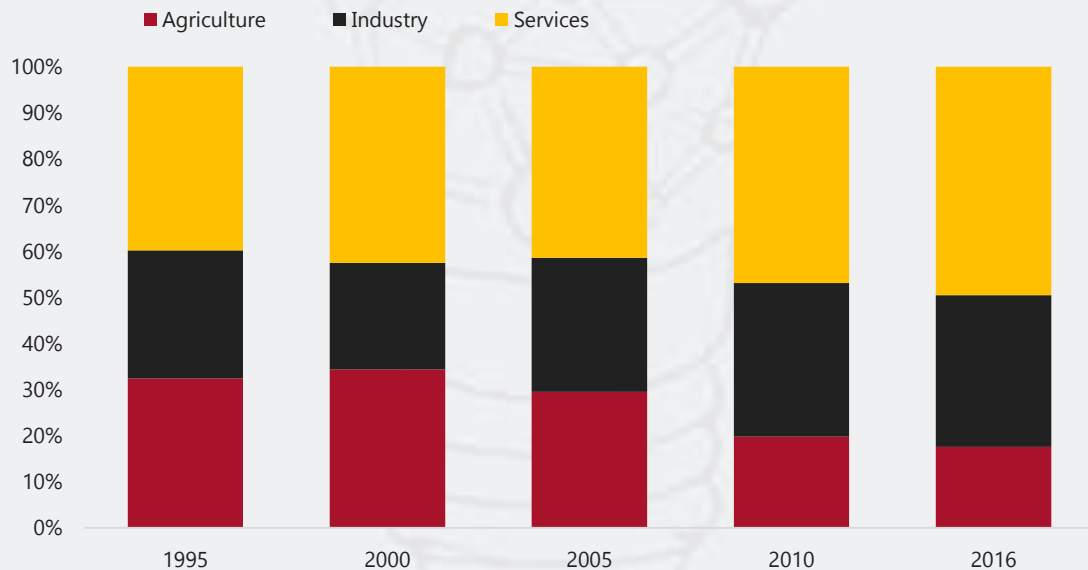
- 2017 was the year of the beginning of reforms and structural transformation of the economy, public administration and foreign policy in Uzbekistan. In the snap presidential elections in Uzbekistan on December 4, 2016, a new head of state was elected. While still serving as acting president, Shavkat Mirziyoyev outlined the main vectors in the country's foreign and domestic policies. In foreign policy, he called regional integration in Central Asia the main priority, and in domestic policy - the liberalization of the economy and reforms in public administration.
- In order to assess the scope of the reforms, it is necessary to know the background of the development of the economy of Uzbekistan during the years of independence.
- **At the very beginning of independence, right up until the second half of the 1990s**, the Government of Uzbekistan took the following major steps to transition to market relations:
 - Large-scale privatization of small and medium-sized enterprises, housing;
 - Social protection of the population was declared as a priority policy of the state;
 - Supporting the development of the private sector, especially in the service sector and small industry;
 - Achievement of grain and energy independence was proclaimed as a medium-term goal of the Government.
 - A phased approach to economic reforms combined with state 's commitment to strong social protection, as well as high world prices for export goods allowed Uzbekistan to avoid deep economic recession and social unrest.
- **Since the second half of the 1990s**, Uzbekistan has followed the policy of import substitution supported by the allocation of public funds (including loans from the state budget and the Central Bank) to the development of priority industries. This policy was also accompanied by an increase in customs duties on a number of imported consumer goods.
- By the end of the 1990s, the economy of Uzbekistan was subjected to a number of external shocks, including global financial crisis of 1997-1998, the Russian crises in 1998-1999, and a fall in world prices for basic exports (including cotton). GDP growth slowed and averaged 4.1% in 1998-2001, and the inflation rate was 30% -45%. In response, the Government tightened the monetary and fiscal policy, through increased control of tax collection, stricter control over the level of imports and reduced access to the conversion of the national currency.
- **By the beginning of the 2000s**, macroeconomic stability was achieved in Uzbekistan and a qualitatively new stage of economic development began. At this stage, macroeconomic stability and further accumulation of resources allowed the Government to implement a number of large-scale social reforms aimed at investing into the education, health care and other related sectors, and establish the Fund for Reconstruction and Development of Uzbekistan (FRDU) for monetary sterilization and economic development in case of external economic shocks.
- **During the 2000s**, a systematic macroeconomic adjustment consisting of tight fiscal policy, a reduction in the budget deficit, and a balanced foreign borrowing policy helped improve external debt performance and continue to implement a number of industrial projects.

External debt, as% of GNP. Source: WB, 2018

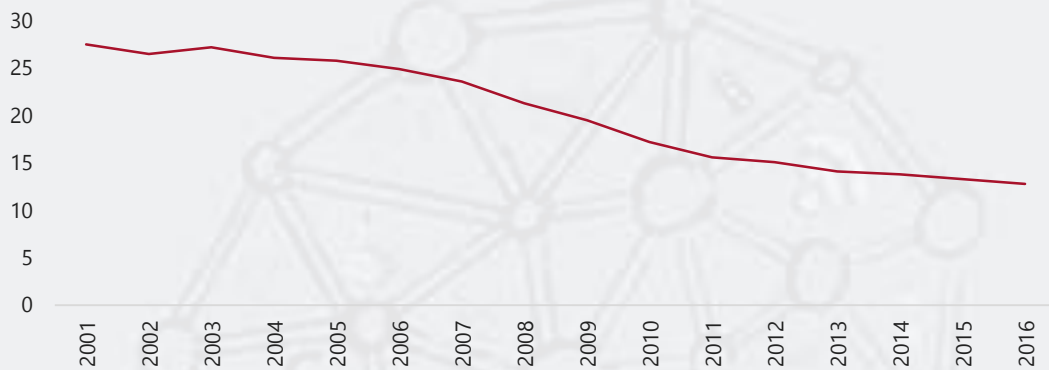


- Significant industrialization of the economy was observed due to the increase of foreign investments in traditionally state sectors such as oil and gas and telecommunications. So, by 2010, the volume of foreign direct investment (FDI) amounted to 944 million dollars, compared with 88 million dollars in 2005. In this period, the average annual GDP growth was fixed at 8%, the structure of GDP began to be dominated by industry and services (compared to agriculture), and the poverty rate declined from 26% to 18%.
- Despite significant progress in economic growth and poverty reduction, the flow of labor migrants to Russia and neighboring Kazakhstan has increased dramatically. These trends indicate an imbalance in the labor market, which will be discussed below.

GDP structure. Source: State Statistics Committee of Uzbekistan, 2018

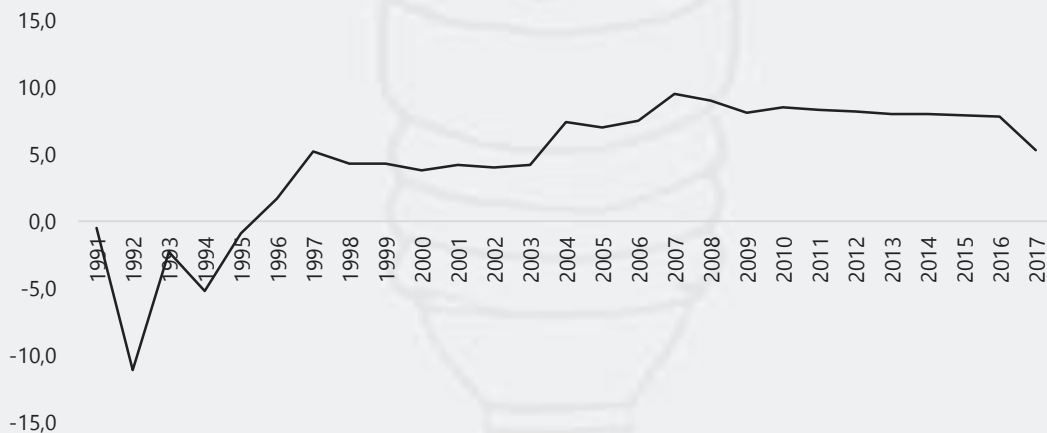


The poverty level, calculated on the consumption of 2,100 kcal per day. Source: WB, 2018



- The observed growth in GDP was largely ensured by:
 - the growth of remittances of labor migrants;
 - sustainability of public investment and growth of domestic consumption;
 - high world prices for the main exports of Uzbekistan as gold, copper, cotton, and natural gas;
 - further diversification of goods exported, such as industrial goods (petroleum products, automobiles, chemical products, metals, processed products, textiles).
- **Since 2012**, the rate of economic growth in Uzbekistan has begun to decline gradually due to a fall in prices for major exports and a number of events in 2014 as an oil crisis, devaluation in Russia and Kazakhstan. Thus, there was a drop in incomes of migrants, together with a decrease in export earnings. In response, the Government continued to implement state programs at the expense of national commercial banks, the FRDU and loans from international financial institutions. At the same time, the Government continued the policy of monetary restraint by reducing access to the conversion of the national currency and continuing a tight fiscal policy.

GDP growth rates. Source: State Statistics Committee of the Republic of Uzbekistan



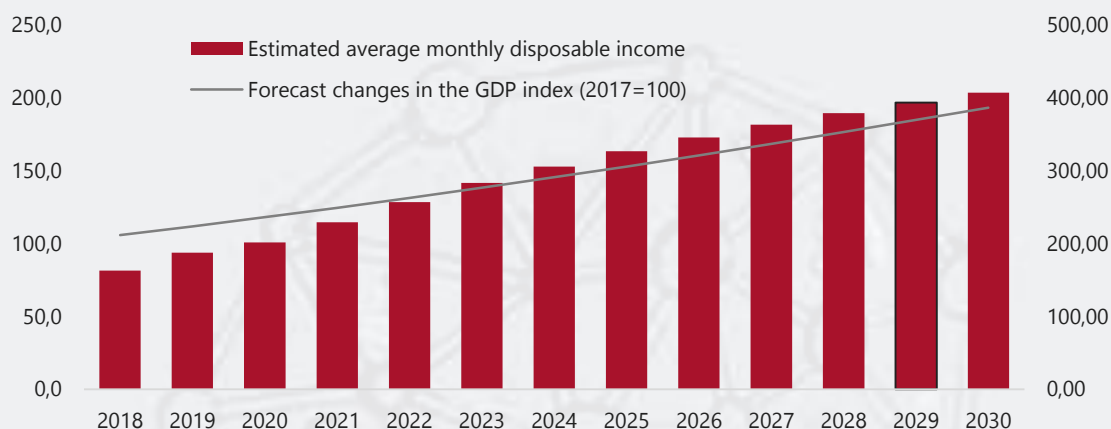
- Despite the macroeconomic successes achieved, a number of issues that hampered the development of the private sector and the business sector remained unresolved in the above-discussed period. So the results of many studies have revealed that the private sector often faced a number of problems that not only did not allow increasing its effectiveness, but often forced to move into the informal sector. Among the persistent problems during these periods were access to cash and freely convertible foreign currency, mandatory payments to various funds, excessive interference of regulatory and supervisory bodies in business activities, the removal of property and non-transparency of legislation, and exhausting licensing and authorization documents restricting the development and competitiveness of business.
- **Since 2014**, reacting to a number of unfavorable external shocks, as a result of which the volume of exports has decreased, commodity prices have declined, and the volume of remittances has decreased, the black market exchange rate has sharply increased and exceeded the official rate by more than 100 percent, exposing the presence of large-scale basic distortions in the economy.
- **At the end of 2016**, the new president of Uzbekistan, Shavkat Mirziyoyev, embarked on the most decisive steps in implementing reforms, realizing in the country the real and vital socioeconomic and political transformations that the country so badly needed. In particular, Uzbekistan has entered a new stage of development since that period, which marks the beginning of the era of reforms in all spheres of public life envisaging the creation of necessary conditions in the sphere of public administration and business, the introduction of fundamental innovations in the dialogue with the people.
- Uzbekistan is currently experiencing significant transformations as a result of reforms implemented within the framework of Action Strategy on the five priority development directions of the Republic of Uzbekistan in 2017-2021. This is one of the biggest political, economic and social reforms in the whole history of the country, which received the support of many world political and economic leaders, including the UN Secretary General, the IMF Managing Director, the President of the World Bank and many others.
- The government has undertaken a number of key changes in economic policy related to currency liberalization, the revision of trade and tax policies. In particular, since the beginning of 2017 the following economic reforms have been or are being carried out:
 - liberalization of the foreign exchange market and unification of multiple exchange rates in September 2017;
 - tax and customs reforms aimed at ensuring the country's openness to trade and investment;
 - administrative reforms, the likely decentralization of local authorities and the development of public-private partnerships;
 - financial sector reforms;

- reform of state companies, including support or conversion of inefficient enterprises and production facilities, simplification of business conditions, stimulation of exports for enterprises, abolition of monopoly on export of fruit and vegetable products, reform of the automobile complex;
 - creation of favorable conditions for inflow of foreign investments;
 - Integration of the economy of Uzbekistan and neighboring countries of Central Asia with the aim of increasing interregional trade, creating regional supply chains, restoring interconnected regional energy and transport networks, and settling the disputes on water use that existed in the region for centuries.
- Also, thanks to the measures implemented within the framework of the Action Strategy for the five priority development directions of the Republic of Uzbekistan in 2017-2021, last year the "Tashkent" Stock Exchange merged into the international capital markets. This opened the way for societies to place assets in foreign financial spaces.
 - At the end of 2017, the population of Uzbekistan for the first time had the opportunity to buy shares that are sold through an initial public offering (IPO). In December 2017, over 4.5 million shares of the stock company "Quartz" were put up for sale. Shares are sold through technology of the initial public offering (IPO) taking into account the priority of the highest proposed purchase price.
 - ***For reference:*** in 2017 the total turnover of corporate securities (shares, bonds) in Uzbekistan was fixed at 22.2 trillion soums, which is 8.8% of the GDP of the republic. For example, this indicator is on average in the Eurozone and Asia - 65%, North America - 140%, in the world as a whole - 98%.
 - The next step in this direction was the placement on the London Stock Exchange of bonds denominated in Uzbek soums by the International Finance Corporation (IFC) in May 2018. This transaction is the first of its kind operations with securities in Uzbek soums in international capital markets, which will undoubtedly positively affect the image of the country and stimulate interest of institutional investors to Uzbekistan.
 - In general, the Government of Uzbekistan, in order to mitigate the negative consequences of reforms for general population, is trying to implement step-by-step reforms in all spheres of public life, in particular in public administration, the judicial and legal system, socio-economic development and international relations, without applying the liberalization scenario as "shock therapy".
- **PERSPECTIVES OF REFORMS AND FORECASTS OF THE GENERAL DEVELOPMENT OF THE COUNTRY**
 - **Reform of the tax system.** In order to bring the tax system in line with analogues in developed countries, reduce the tax burden, strengthen the stimulating role of taxes, increase taxpayer confidence, and radically improve tax administration in 2018, a draft concept of tax reforms was developed. In Uzbekistan, the reorganization of tax authorities, the cancellation or consolidation of duplicate taxes is envisaged; a real reduction in the tax burden, improvement of tax legislation, introduction of a tax holiday mechanism for companies (entrepreneurs) into practice, etc. It is expected that by 2020 the country will be fully transformed into a mechanism that is understandable for foreign investors and encourages them to invest in the economy of Uzbekistan.

- **Uzbekistan's accession to the WTO.** Currently, accession to the WTO is one of the priorities of Uzbekistan's foreign economic policy. This issue is considered as one of the key factors in improving the international image of the country. In accordance with the Memorandum and the road map signed in April 2018, Korea will provide technical, advisory and expert support in the process of Uzbekistan's accession to the WTO. At the moment, Uzbekistan participates in the work of the organization as an observer state, and it is planned that within the next 5 years the country will become a full WTO member.
- **Stock market.** It is expected that reforms in stock market will be initiated in 2018-2019. In particular, measures will be taken to reform the national stock market on the basis of a critical analysis of the state share management system and the study of successful international experience, the criteria will be developed for evaluating the activities of the Center for coordination and development of the securities market, changes will be made to the legislation to increase the liquidity of the stock market, as well as conditions will be created for domestic and foreign investors to invest in securities of Uzbek companies, with subsequent public offerings of the shares by means of IPO and SPO.
- **Real sector.** The Government of Uzbekistan intends to create favorable conditions for the development of private entrepreneurship by simplification of procedures and acceleration of the process of the realization of state property, elimination of bureaucratic barriers in their privatization, organization of the production of competitive goods and services on the privatized objects. As a result of the implementation of long-term and predictable policy, the formation of a transparent business and investment climate, as well as the development of the securities market by 2021, a radical reduction of the state's share in the authorized funds of economic societies and an increase in their investment attractiveness will be ensured.
- **High share of economically active population as an additional factor of economic growth.** In the last two decades, economically active population is rapidly growing in the country, and currently, the labour market continues to increase annually by about 500,000 people seeking employment opportunities. Today, the share of the working-age population in the total population is about 60% and this figure will remain extremely high over the next few decades. This opens up a unique opportunity for Uzbekistan to realize its aspirations to use a large number of economically active population for further economic growth and to achieve the status of a country with a higher income level than the average within the life of one generation. At the same time, the authorities are fully aware that if the creation of jobs does not keep pace with the rapid growth in the supply of labour, it will lead to high levels of unemployment and mass labour migration, especially in rural areas, as well as increased dissatisfaction.
- **Economic growth.** In 2018-2019, continuation of stable GDP growth at around 5-6 percent is projected. However, in the long run, Uzbekistan's economy is expected to grow at a faster pace than its neighbors and above the global average. This will be facilitated by a favorable environment of external demand, thanks to the ongoing reforms and the expected normalization of the crop, as well as a high level of domestic and foreign investment in the country's economy.

Forecast of growth in disposable income and GDP index in 2018-2030, GDP 2017 = 100.

Source: Authors' calculations



- **International trade.** It is expected that due to ongoing reforms to liberalize imports, the surplus of foreign trade turnover will be replaced by a small deficit by 2019. At the same time, the volume of exports is expected to grow at a steady pace, and it is possible that its growth may exceed expectations. From 2021 it is forecasted to achieve a positive balance and a moderate increase in foreign trade turnover due to an increase in the volume of exports and the inflow of foreign direct investment.
- **Inflation.** It is forecasted that inflation will remain at an elevated level in 2018 (13-14% per annum), which is quite normal at an early stage of liberalization of the economy, characterized by distortions. Also in practice, high inflation is typical for countries at an early stage of transformation in the transition process. It is expected that during 2019-2020, the inflation rate will gradually decrease to a single digit.

Uzbekistan: Selected economic indicators, 2015-2021

Indicators	2015	2016	2017	Forecast			
				2018	2019	2020	2021
Real GDP growth (in%)	7.9	7.8	5.3	5.0	5.0	5.5	6.0
GDP per capita (in US dollars)	2,124	2,094	1,491	1,238	1,455	1,700	2,000
Inflation (in%)	8.4	7.9	14.4	18.0	12.0	9.0	7.0
Population size (million people, beginning of period)	31.3	31.8	32.1	32.6	33.4	33.9	34.4
Gross official reserves (in billions of dollars)	24.3	26.5	28.1	29.2	29.5	30.0	30.0
External debt (in billions of dollars)	11.8	13.0	15.6	15.7	18.2	21,0	22,0
The exchange rate (in soums for \$ 1, at the end of the period)	2,810	3,231	8,120	8,000	8,800	9,500	10,000



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