Uzbekistan

Strong economic growth in 2010 was driven by expanded public investment, increased net exports, and a pickup in workers' remittances. The outlook is for sustained public sector–oriented growth, and continued strong fiscal and external positions. The authorities need to keep a close eye on inflation, though it is expected to remain moderate. Diversification from the commodity and energy sectors, alongside private sector development, would help to generate broad-based and sustained growth.

Economic performance

The economy continued to perform well in 2010, supported by the effects of a fiscal stimulus, the government's medium-term investment program, and the global economic recovery. Growth was driven mainly by industry (including construction) and services (Figure 3.8.1), with estimated annual growth rates of 8.3% and 11.6%, respectively.

In industry, growth was led by the chemical, machinery, light, and food industries, which together expanded by 12.0% and accounted for almost half of total industrial output. These industries benefited from the significant public investment and commercial bank lending provided under the government's 2009–2010 anticrisis and industrial modernization programs. The chemical and machinery industries are also attracting investment from Asia and the Middle East. Construction grew at 8.1%, largely due to government support to rural infrastructure and housing development, as well as greater foreign investment in hydrocarbons.

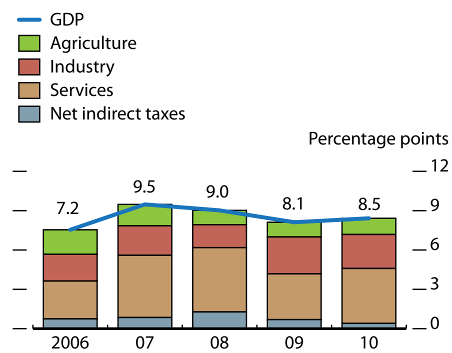
The expansion in services mainly reflected increases in government social spending for health care, especially in rural areas. Favorable weather and higher vegetable crop cultivation led to agricultural growth of 6.8%.

In 2010, the government continued implementing infrastructure programs aimed at developing rural areas and modernizing industry. The Fund for Reconstruction and Development (FRD) and state-owned banks allocated about $6.0 billion. Lending from commercial banks to the economy increased by one-third in 2010. Gross fixed capital investment rose by 9.2%, to the equivalent of around 30% of GDP (Figure 3.8.2). According to the government, about $3.9 billion, or 25.1%, was foreign.

The majority of foreign investment goes into fuel, energy, telecommunications, and automobile manufacturing. The government reported that it plans to attract up to $50 billion in foreign investment during 2011–2015. Notable projects include a joint venture with Daimler on bus assembly and expansion of production lines at GM Uzbekistan (a joint venture between General Motors and the state-owned Uzavtosanoat company). Under government initiatives to encourage use of natural gas in vehicles, a new joint venture between Uzbekistan and the Republic of Korea will construct gas compressor stations for cars.

In February and October 2010, the authorities raised utility prices

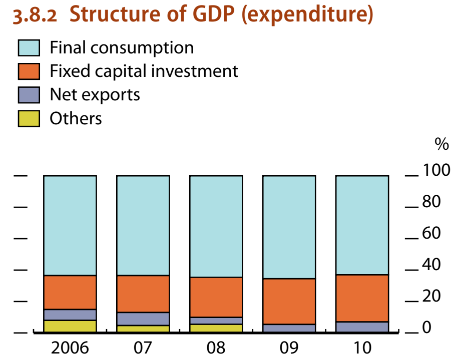
3.8.1 Contributions to growth (supply)



Sources: State Statistics Committee of Uzbekistan; ADB estimates.

Click here for figure data

3.8.2 Structure of GDP (expenditure)



Note: Others refer to statistical discrepancy and changes in stocks.

Sources: Center for Economic Research. *Uzbekistan Almanac 2010*; ADB estimates.

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This chapter was written by Iskandar Gulamov of the Uzbekistan Resident Mission, ADB, Tashkent.

for heating, hot water, and electricity by a cumulative 18%–30% in an attempt to bring them closer to cost-recovery levels. The increases, with depreciation of the local currency and a 30% annual hike in public wages and pensions, put upward pressure on inflation. The central bank sought to mitigate this pressure by slowing broad money growth to 34.6% from its peak of 43.8% in 2009. The government reported year-end inflation of 7.3%. The latest estimate from the International Monetary Fund for average inflation is 10.6% (Figure 3.8.3).

The local currency depreciated by 8.3% against the dollar in 2010. On 1 January 2011, the central bank reduced its benchmark refinancing rate from 14% to 12% to reduce the rates of loans provided under its programs for industrial modernization, rural housing construction, and small and medium-sized enterprises.

The general government budget is estimated to be in balance in 2010. Taking into account the FRD, the consolidated budget is estimated to have a surplus of 2.5% of GDP (Figure 3.8.4). The steep wage and pension hike, greater support for health care, as well as the rural development program have lifted budget spending to an estimated 34.6% of GDP. The government also provided tax exemptions for enterprises operating under investment and localization programs, but revenue gains from commodity exports and the utility price adjustments were enough to offset the increased expenditure.

In line with the policy of reducing direct taxation to encourage economic activity, in 2010 the government reduced the rates of both corporate and personal income taxes by 1 percentage point to 9% and 11%, respectively. The fiscal authorities also reduced the rate of the unified tax paid by micro and small firms from 8% to 7%. The share of direct taxes in GDP decreased from 7.1% in 2008 to an estimated 5.9% in 2010.

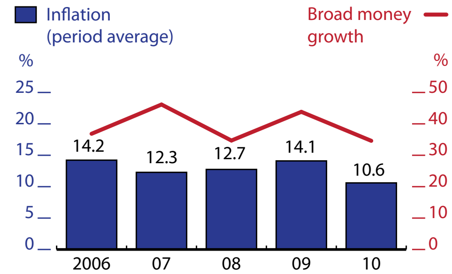
Reflecting the increased infrastructure development and subsequent rise in foreign financing, including government-guaranteed foreign debt, total external debt is estimated to have risen to 14.9% of GDP, slightly above the 2009 figure of 14.6%.

The international prices of gas, cotton, and gold, Uzbekistan's main export commodities, were historically high throughout 2010, leading to goods and services export growth of 10.8%. That growth was also aided by recovery in the Russian Federation, with the share of machinery, including passenger vehicles, in total exports more than doubling in 2010. Stronger growth in the Commonwealth of Independent States sharply boosted foodstuff exports.

The government reported that imports of goods and services fell by 6.8% in 2010. Imports of machinery and equipment, 44% of the total, dropped by 27.3%. Official import restrictions reduced imports, especially from countries in the Commonwealth of Independent States. Reflecting a pickup in global food prices as well as stronger consumption demand, the share of foodstuffs in imports climbed from 10.3% in 2009 to 10.9% in 2010.

Remittances sent to Uzbekistan from the Russian Federation rose by an estimated 22% in 2010 to $1.4 billion (to around 3.7% of GDP), given the economic pickup in that country. Due to improved exports and remittances, the current account surplus is estimated to have increased to 15.6% of GDP in 2010, from 11.0% of GDP in 2009 (Figure 3.8.5).

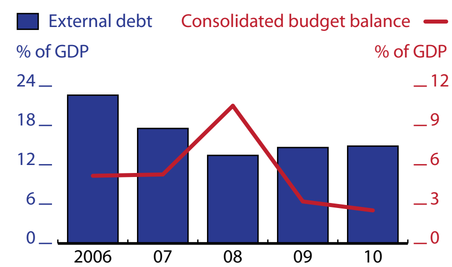
3.8.3 Inflation and money supply



Sources: International Monetary Fund. 2010. *Regional Economic Outlook: Middle East and Central Asia*. October. http://www.imf.org; ADB estimates.

Click here for figure data

3.8.4 Fiscal and debt indicators



Sources: International Monetary Fund. 2010. *Regional Economic Outlook: Middle East and Central Asia*. October. http://www.imf.org; ADB estimates.

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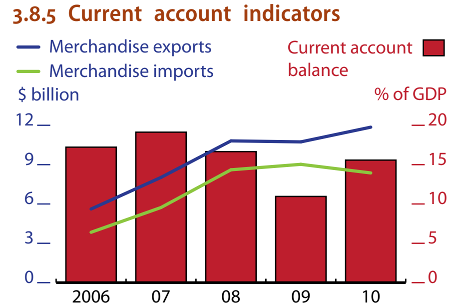
3.8.5 Current account indicators



Sources: International Monetary Fund. 2008. *Article IV Consultation*. July. http://www.imf.org; ADB estimates.

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Economic prospects

Greater investment and infrastructure development will sustain GDP growth at 8.5% in 2011 and 8.4% in 2012. Industry (particularly construction) and services are expected to be the major contributors. Industrial output will be driven by domestic lending and foreign investment, while services will expand in line with higher domestic demand. Increasing lending coupled with favorable international prices will stimulate output of energy, machinery, and metals. Agriculture is expected to be driven by higher vegetable and fruit output, while grain production will improve moderately.

The share of investment in GDP is expected to climb rapidly in the forecast period, partly because the government is seen pursuing the infrastructure development programs faster. On 15 December 2010, it adopted a presidential decree that envisages spending $30 billion on 259 industrial projects and $23.1 billion on new construction in 2011–2015. Most financing for both sets of programs is planned to come from enterprises' own resources, loans from domestic banks, and FRD resources.

The government plans to direct up to 60% of budget spending ($6.2 billion) toward social programs—outlays on which are expected to rise by 14%—at the same time as raising allocations for investment (by 37%). It is also seen further reducing the tax burden and strengthening revenue collection. The consolidated budget, including the FRD, is forecast to post a surplus of 2.4% in 2011 and 2.0% in 2012.

Higher public sector wages and social payments alongside a gradual recovery in remittance inflows will sustain domestic consumption, as will government plans to create many jobs through infrastructure. Higher import costs, a more accommodative fiscal policy, and further depreciation of the local currency will stoke price pressures in 2011–2012. To counter them, the authorities are likely to adopt a monetary policy that slows money supply growth. Inflation is forecast at 8.8% in 2011 and 8.5% in 2012.

International prices for gold and cotton are seen peaking in 2011, but staying high. Uzbekistan's export prices for natural gas, which have approached international levels, are likely to stay at these high levels. Exports are forecast to grow at 14.0% in 2011 and 3.1% in 2012, supplemented by a gradual improvement in remittance inflows. The steep rise in public investment will likely offset the slower export growth in 2012 in terms of contribution to GDP.

Growth in imports will be driven by expansion of infrastructure development and by increases in global energy and food prices. Since machinery and equipment are the main import items, the post-2011 investment surge will drive imports even higher. Import growth is therefore put at 11.9% in 2011 and 16.3% in 2012. The current account surplus is projected at 16.3% and 12.6% of GDP.

The downside external risks to the forecasts are related to the pace of economic recovery in Uzbekistan's main trading partners as well as uncertainty in global financial markets. The immediate challenge is to manage rising pressures from fiscal expansion and global food price increases. To prevent unwanted fiscal-led pressure on monetary policy, the authorities are ready to adapt the structure of budget expenditure and the pace of nominal depreciation of the currency.

3.8.1 Development challenges

With one eye on the long-term goal of diversifying the economy, the government has designated 2011 as the year of small businesses and private entrepreneurs.

According to official statements, these two groups contributed more than half of total GDP and employed more than 70% of the total labor force in 2010. The central bank reported that total lending to both groups jumped by 40% that year to $1.7 billion. As well as lowering taxes, the government's program for 2011 targets better access to capital for them and simpler reporting requirements.

Sources of export income, too, need to be broadened and natural resources prudently managed, as the current resource-based approach is susceptible to volatility in global commodity prices.

Effective banking supervision and improved prudential banking requirements will help to guard against potential risks associated with rapid credit growth and greater commercial bank lending to state-owned enterprises.

Improving access to credit for small and medium-sized enterprises will widen the range of banking assets while benefiting the broader population through job opportunities.

3.8.1 Selected economic indicators (%)

	2011	2012
GDP growth	8.5	8.4
Inflation	8.8	8.5
Current account balance (share of GDP)	16.3	12.6

Source: ADB estimates.