Uzbekistan

Growth accelerated in 2011, driven by net exports, state-led investments, and remittances. With lower non-oil commodity prices in 2012, economic growth will be sustained by public investment and increasing foreign investment. The key downside risk is a deteriorating economic environment in the euro 20 and the Russian Federation. To reduce risks from reliance on commodity exports, the economy needs to diversify beyond the natural resources sectors and expand the private sector.

Economic performance

Reflecting the favorable external environment, sustained public investment, and rising private consumption bolstered by remittances, Uzbekistan's strong economic performance continued in 2011 with GDP growth of 8.3% (Figure 3.8.1). As in previous years, industry (including construction) and services were the main contributors to GDP growth, with estimated growth rates of 6.7% and 12.7%, respectively.

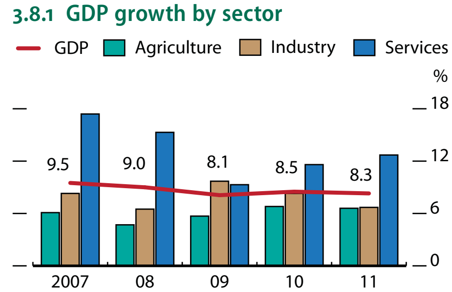
Industrial growth declined to 6.7% from 8.3% in 2010, mainly due to a slowdown in the fuel subsector, where a decline in natural gas output kept growth to 0.3%. Nevertheless, all subsectors grew collectively by 11.9%, in particular machinery and equipment, chemicals and petrochemicals, construction materials, and the food industry, reflecting strong external demand for metals and petrochemicals and continued industrial development. Construction grew by 8.5%, reflecting higher public construction, which offset a slowdown in foreign investment-related construction activities.

As in 2010, services were again a main source of growth, with retail trade, communications, and financial services recording a combined growth rate of 22.3%, supported by strong domestic demand, in particular, rising private consumption. The agricultural sector grew by 6.6%, supported by fruit and vegetable production and livestock breeding.

On the demand side, rising remittances, increased domestic lending, and wage and pension hikes boosted private consumption. Gross fixed capital formation increased by 11% in nominal terms, to 26% of GDP, as bank lending for investment rose by one-third (Figure 3.8.2). Most investment went to industry, for purchases of capital goods.

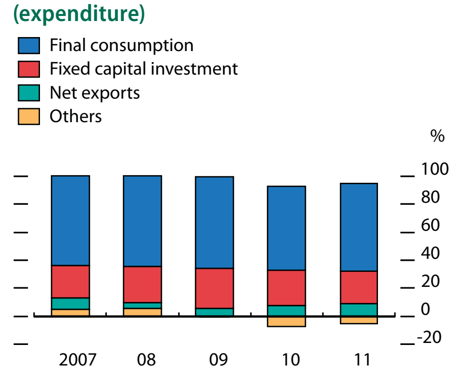
Estimates of inflation range from the government's 7–9% to 13.1% from the International Monetary Fund, with the latter above 2010's outturn of 9.4%. Inflation in 2011 reflected public sector and pension increases in August and December, totaling 26.5% since December 2010, with high foreign exchange inflows, rapid credit growth, local currency depreciation, and increased private and public spending.

3.8.1 GDP growth by sector



Sources: State Statistics Committee of Uzbekistan; ADB estimates.

3.8.2 Structure of nominal GDP (expenditure)



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

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

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

It is believed that 0.3% output growth of the fuel sector in 2011 and subsequent substantial increases in fuel costs have provided additional inflationary pressures.

The central bank attempted to curb inflation by issuing certificates of deposit (equivalent to 40% of the existing stock) in order to sterilize excess liquidity, while the government absorbed $1.6 billion of export revenues into the Fund for Reconstruction and Development, Uzbekistan's sovereign wealth fund.

The augmented budget, which comprises the official budget plus the surplus from this fund, is estimated to have recorded a surplus of 3.2% of GDP. Revenue gains from higher commodity prices and improved tax administration (taking revenue to an estimated 38.5% of GDP, from 37.1% in 2010) offset the impact on spending of wage and pension increases, higher social outlays, and the rural development program (overall expenditure climbed to 35.3% of GDP, from 34.4% in 2010).

The central bank's issuance of certificates of deposit helped reduce broad money growth from 52.4% in 2010 to a still high 27.7%. Banks benefited from heavy government injections aimed at strengthening their capital and increasing lending. Bank lending to small and medium-sized enterprises and private entrepreneurs reached $2.8 billion, a 50% increase from 2010. In August 2011, Moody's reconfirmed its rating for the banking system as stable, following an upgrade a year earlier.

The central bank continued to intervene in the foreign exchange market, with the aim of depreciating the local currency—the sum—to promote competitiveness. Depreciation of the Russian ruble and Kazakh tenge against the US dollar added downward pressure on the rate. By year-end the sum depreciated by 8.6% against the dollar, more than in 2009 and 2010 (Figure 3.8.3).

An improved trade balance and higher remittances helped raise the current account surplus to 8.1% of GDP from 6.6% in 2010 (Figure 3.8.4). Exports of goods and services rose by 28.6% to $15.6 billion, as international prices for gold, cotton, copper, and natural gas reached record levels, and strong consumer demand in the Russian Federation contributed to a 25% rise in automobile exports by GM Uzbekistan.

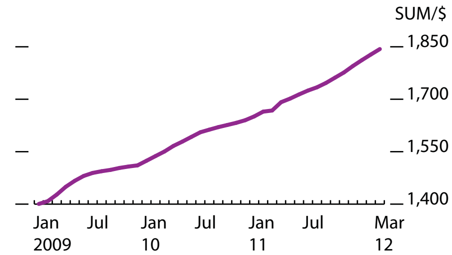
Imports of goods and services rose by 26.5% to $14.0 billion, as continued state-led public infrastructure development and industrial modernization required more imported capital goods. Remittances grew sharply, particularly from the Russian Federation, as the Russian economy improved.

The government reported foreign investment inflows of $2.9 billion, of which 79% was for foreign direct investment (FDI), mainly in the fuel, energy, petrochemical, and automobile manufacturing sectors. External debt is estimated to have risen to 17.5% of GDP from 14.7% of GDP at end-2010, as the public investment program is increasingly being financed with foreign loans (Figure 3.8.5).

Economic prospects

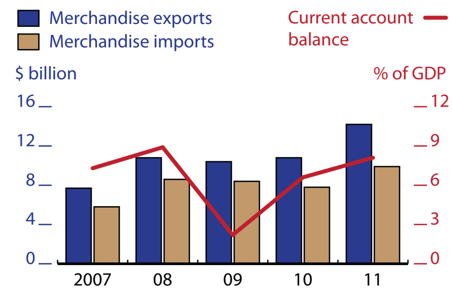
GDP is forecast to grow by 8.0% in 2012 and 7.9% in 2013, as rising state-led investments are expected to offset a decline in exports. Industry and services are expected to be the major contributors to economic

3.8.3 Exchange rate



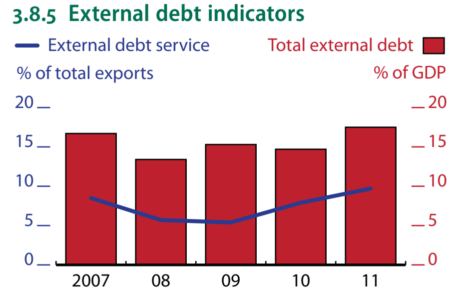
Source: Central Bank of Uzbekistan. http://www.cbu.uz/ (accessed 28 March 2012).

3.8.4 Current account indicators



Sources: International Monetary Fund. 2011. *Regional Economic Outlook: Middle East and Central Asia*. October. http://www.imf.org; ADB estimates.

3.8.5 External debt indicators



Sources: International Monetary Fund. 2011. *Regional Economic Outlook: Middle East and Central Asia*. October. http://www.imf.org; ADB estimates.

growth. Industrial output will be supported by higher domestic lending and foreign investment, while services will be driven by higher domestic demand, especially from the public sector. Higher vegetable and fruit output should boost agriculture relative to 2011.

On the demand side, continued public investment should be a key driver. Gross fixed capital formation is forecast to rise by 9.3% in 2012 in nominal terms, with investment exceeding 30% of GDP. The government is implementing a $47.3 billion Industrial Modernization and Infrastructure Development Program in 2011–2015, with significant investment planned in oil and gas, electricity generation, chemicals, metallurgy, and other strategic sectors.

Domestic consumption will be supported by expected increases in public sector wages and pensions, and additional measures—probably further wage increases and welfare payments—are likely to be taken if the slowdown in the eurozone and the Russian Federation appears to be hampering growth. Nevertheless, lower remittances are expected to moderate growth in private consumption, which is forecast to rise, in nominal terms, by 8.0% in 2012 and 9.0% in 2013.

Inflation is expected to come in at about 9.5% in 2012 and 9.0% in 2013, as global commodity prices decline, although continuing currency depreciation will keep import prices high (Figure 3.8.6). The authorities are also expected to limit measured inflation through sterilization operations and domestic price controls.

The official government budget, adopted in November 2011, projects a deficit of around 1% of GDP in 2012; the augmented budget is forecast to show surpluses of 4.0% in 2012 and 3.2% in 2013 (Figure 3.8.7). The official budget envisages substantial tax reductions, with the goal of reducing the ratio of tax revenue to GDP by 0.7 percentage points in 2012, although commodity-based revenue is expected to grow strongly, and additional revenue will come from new excise taxes on imported vegetable oil and domestically produced jewelry. Augmented budget revenue is forecast at 39.0% of GDP in 2012 and 38.3% in 2013. Almost 60% of expenditures will go to social security, welfare, health care, education, and culture. Augmented budget expenditures are projected at 35.0% of GDP in 2012 and 35.1% in 2013.

Money growth is expected to accelerate to 30% in 2012 and 33.6% in 2013, as public wages and pensions rise and banks increase their lending. Further increases in official reserves (at least in 2012) and continued foreign exchange intervention to depreciate the currency will increase reserve money, offset partly by further central bank sterilization operations.

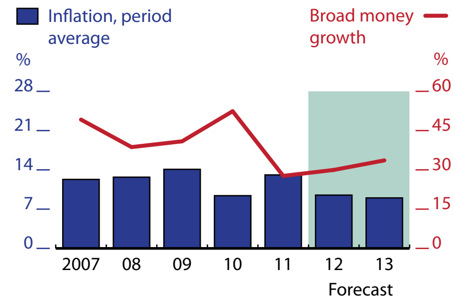
The current account surplus is forecast to decrease to 7.5% of GDP in 2012 and 6.0% of GDP in 2013, as the trade balance weakens (Figure 3.8.8). Declining international prices for the country's main exports, excluding natural gas, coupled with weaker external demand, will hamper export performance, with exports forecast to rise moderately in 2012 and decline in 2013. Recession in the European Union will likely lower growth in the Russian Federation, Uzbekistan's main trading partner, reducing exports, especially for automobiles and food, and remittances. Moreover, an expected growth slowdown in the People's Republic of China is expected to reduce key metal and cotton exports.

3.8.1 Selected economic indicators (%)

	2012	2013
GDP growth	8.0	7.9
Inflation	9.5	9.0
Current account balance (share of GDP)	7.5	6.0

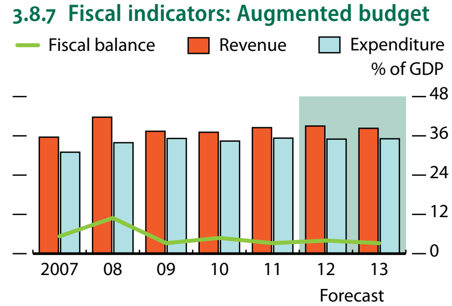
Source: ADB estimates.

3.8.6 Inflation and money supply



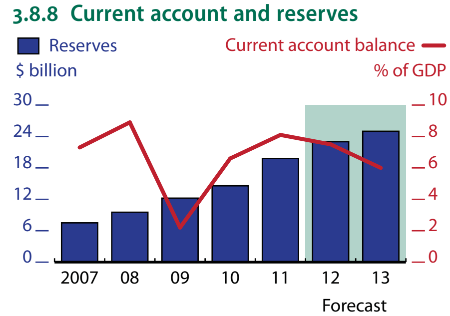
Sources: International Monetary Fund. 2011. *Regional Economic Outlook: Middle East and Central Asia*. October. http://www.imf.org; ADB estimates.

3.8.7 Fiscal indicators: Augmented budget



Sources: International Monetary Fund. 2011. *Regional Economic Outlook: Middle East and Central Asia*. October. http://www.imf.org; ADB estimates.

3.8.8 Current account and reserves



Sources: International Monetary Fund. 2011. *Regional Economic Outlook: Middle East and Central Asia*. October. http://www.imf.org; ADB estimates.

Import growth is forecast to slow to 8.3% in 2012 and 2.8% in 2013, despite infrastructure spending and the industrial modernization program, because of the projected moderation in imported food prices and tighter import controls, particularly on imported consumer goods. Gross international reserves are forecast to increase further in 2012 and 2013 (to $23.0 billion and $25 billion, respectively), according to ADB estimates, reflecting continuing current account surpluses and net capital inflows.

Reflecting increasing foreign borrowing for industrial modernization and infrastructure development, external debt is forecast to reach 20.2% of GDP and end-2012 and 22.8% a year later.

Policy challenge—developing the private sector

Uzbekistan's private sector will play a greater role in economic development as the economy moves toward middle-income status. The government has reported that small businesses accounted for 54% of GDP in 2011, which is at par with international averages, but the role of entrepreneurs in key areas of economic activity has yet to develop (Figure 3.8.9).

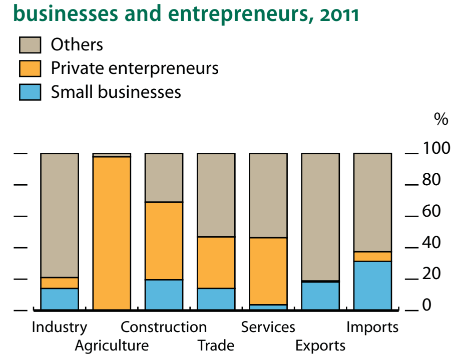
Policies and investment to improve the business climate, promote the private sector, and strengthen infrastructure and trade need to be reinforced for a more diversified and sophisticated export sector and to accelerate the economy's transformation.

Improving the business climate is urgently required to develop the private sector, especially for the many small businesses that represent the overwhelming share of legal entities and provide most national employment. A more favorable business climate would promote diversification and the growth of new firms. It would also facilitate private sector participation in the infrastructure and other strategic sectors, as these are gradually opened to private firms. (The private sector is already involved in repairing and maintaining public roads, and its share in road freight transport reached 72.2% in 2010 from 58.7% in 2005.)

Uzbekistan is ranked overall 166 out of 183 economies in the World Bank's 2012 *Doing Business* report (and lowest in the trading across borders category). Accelerating regulatory reforms to attract investors, ensuring access to finance and foreign exchange, simplifying customs procedures, and continuing the efforts to offer competitive factor prices would help transform the national economic landscape and sustain economic growth.

Other key measures include further steps to reform the tax regime, liberalize regulations for small firms, increase access to external financing in the banking and nonbank sectors, and develop the securities market. Finally, although the country has taken steps toward decentralizing some activities in public administration, further reforms in this area will multiply the benefits of economic growth.

3.8.9 Economic participation of small businesses and entrepreneurs, 2011



Sources: State Statistics Committee; ADB estimates.