Uzbekistan

The economy grew by 8.2%, nearly as quickly as in 2011, driven by strong performance in all production sectors, continuing public investment, and high remittances and public sector wage increases, which boosted private consumption. Growth is forecast to slow only slightly in 2013 and 2014, while the current account remains in surplus. A more sophisticated and diversified industrial and export base is needed to sustain growth and expand employment over the longer term.

Economic performance

Despite weaker external demand, the economy again performed strongly. GDP grew by 8.2%, according to official data, driven by public investment and private consumption. The main supply-side contributors to growth were services, which grew by 10.4%, and industry including construction, which grew by 8.0% (Figure 3.8.1).

Industry growth was driven mainly by machinery, fuel, and light industry. Services played a larger economic role, due to strong performances by information and communication technology, finance, and trade and catering. Agriculture grew by 7%, primarily reflecting a larger cotton harvest and expanded livestock breeding.

On the demand side, private consumption rose by 6.0%, as a result of higher public sector wages and pensions, expanded remittances, and increased domestic lending. Gross fixed capital formation increased by 11.6%. (Data for total investment are not available, because there is no information on changes in stock inventories.) Public investment rose by 16.7%, improving on the 11.3% increase in 2011, as the government further expanded investment to support ongoing industrial modernization and infrastructure development. Most public investment was to overhaul key industrial sectors and construct new housing.

The government reported that inflation in 2012 remained within the official target of 7%. An alternative estimate by the International Monetary Fund is 12.9%. Inflationary pressures mainly reflected currency depreciation, wage and pension increases, and higher administrative prices for fuel, utilities, and bread, which were instituted toward achieving cost recovery. The central bank responded by tightening monetary policy, especially in the second half of the year, through sales of certificates of deposit on the open market, though the policy rate remained unchanged. An increase in net foreign assets was offset by accumulating government deposits, including in the Fund for Reconstruction and Development (FRD), a sovereign wealth fund. As a result, broad money growth slowed to 25.0% from 32.3% in 2011 (Figure 3.8.2).
The central bank continued to intervene in the foreign exchange market with the aim of depreciating the local currency—the sum—to promote competitiveness. By year-end the sum had depreciated by almost 10% against the dollar.

Fiscal policy remained broadly unchanged in 2012. The consolidated budget, including large surpluses from the FRD, is again estimated to have recorded an overall surplus, equal to 3.1% of GDP. Revenue gains from historically high prices for key export commodities (mainly precious metals) and improved tax administration offset expenditures to cover wage and pension increases and higher social outlays. Revenues equaled 36.7% of GDP and expenditures 33.6% (Figure 3.8.3).

The current account surplus narrowed to an estimated 4.7% of GDP from 8.1% in 2011 as the trade surplus decreased (Figure 3.8.4).

Exports of goods and services declined by 5.1%, reflecting weaker external demand and declines in international prices for Uzbekistan’s major export commodities: cotton, copper, and natural gas. Exports of cotton, foodstuffs, chemical, metals, and machinery all fell in 2012. However, an 81% rise in exports of energy products, primarily natural gas, limited the overall decline in exports.

Imports of goods and services rose by 9%, as continued state-led infrastructure development and industrial modernization required more imports of capital goods and services. Remittances and compensation from abroad, included in the income account, grew sharply, particularly from the Russian Federation, which totaled $5.6 billion. This was the highest amount since independence, reflecting strong demand for construction labor (Figure 3.8.5).

The government reported foreign investment inflows of $2.5 billion, mainly into oil and gas, petrochemicals, and automobile manufacturing. External debt is estimated to have increased modestly to 17.8% of GDP at the end of 2012 from 17.4% at the end of 2011, as the public investment program is increasingly being financed by foreign loans (Figure 3.8.6).

Economic prospects

GDP growth is forecast at 7.5% in 2013 and 8.0% in 2014, driven by state-led investment and domestic consumption. Industry and services will continue to be the main supply-side drivers of economic 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. Agriculture is projected to post healthy growth, albeit less than the 8-year high observed in 2012.

Backed by a large FRD surplus, the government is expected to continue increasing public investment in infrastructure development, industrial modernization, and housing. The government investment program for 2013 envisages projects equal to 24.7% of GDP. Gross fixed capital formation is forecast to rise by 10% in 2013 and 11% in 2014.

The 2013 program will be implemented under the framework of the $47.3 billion Industrial Modernization and Infrastructure Development Program for 2011–2015, financed through a combination of external financing, domestic investment, and FRD resources. The program...
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aims to add more value in manufacturing and raise exports of oil, gas, petrochemicals, and other chemicals. In addition to the ongoing $4.0 billion Surgill Natural Gas Chemicals Project, the program includes developing a $4.0 billion facility to liquefy natural gas in the Kashkadarya Region.

As in 2012, the government is expected to implement measures in 2013 and 2014 to augment consumption, most likely by raising public sector wages, welfare payments, and pensions. Private consumption is forecast to rise by 7.0% in 2013 and 8.0% in 2014, reflecting these developments, planned expansion of retail credit from banks, and the expectation of sustained remittances.

Inflation is forecast at 9.5% in 2013 and 9.0% in 2014. Anticipated declines in global food prices, lower import costs, the lagged effect of monetary tightening in 2012, and continued tight monetary policy are expected to slow inflation, despite planned wage and pension increases and further growth in net foreign assets.

Fiscal policy is expected to relax slightly in coming years, with the augmented budget surplus expected to decline to 2.9% of GDP in 2013 and 2.6% of GDP in 2014. Revenues from commodity exports will likely remain robust, albeit growing less rapidly than in 2011 and 2012. Revenues are forecast to equal 31.0% of GDP in 2013 and 30.2% in 2014. Supplementing these revenues will be FRD transfers projected at 5.5% of GDP in 2013 and 5.2% in 2014. On the expenditure side, the budget strongly emphasizes welfare and social development. Almost 60% of all expenditure is allocated to social security, welfare, health care, education, and culture. Augmented budget expenditure is forecast at 33.6% of GDP in 2013 and 32.9% in 2014.

Money supply growth is expected to remain at 25% in 2013 and 24% in 2014, as the government increases wages and pensions. Further build-up in the central bank’s net foreign assets, at least to mid-2013, and continued foreign exchange intervention to depreciate the local currency will tend to raise foreign reserves. Nevertheless, the authorities are expected to keep monetary policy tight and continue the accumulation of government deposits and liquidity-mopping operations.

The current account surplus is forecast to shrink further, to 4.3% of GDP in 2013 and 3.2% of GDP in 2014, as the trade surplus dwindles (Figure 3.8.7).

Falling external demand and international prices for the country’s main export commodities will adversely affect export performance. The key downside risks are economic slowdown in the European Union or the Russian Federation and, in the People’s Republic of China, uncertain demand for imports. Weaker consumer demand in these countries would suppress trade and remittances. Merchandise exports should rise moderately, by 6.9% in 2013, before declining by 1.0% in 2014.

Merchandise imports are projected to rise gradually, by 9.1% in 2013 and 4.2% in 2014. Demand will come mostly from public infrastructure spending and the industrial modernization program. Lower global commodity prices will reduce import payments, as will greater import controls. Early in 2013 the government adopted a decree that effectively restricted imports by imposing additional procedures and controls on a number of consumer goods.
Reflecting higher foreign borrowing for industrial modernization and infrastructure development, external debt is forecast to reach 19.3% of GDP at the end of 2013 and 20.8% at the end of 2014—still modest by international standards.

Policy challenge—diversifying exports and liberalizing external trade

Although continued government investment in infrastructure and industrialization will promote growth, Uzbekistan needs to develop a more sophisticated and diversified industrial and export base to sustain growth and expand employment over the longer term. Moreover, infrastructure development and industrial modernization programs are themselves influenced in the long run by exports, as government investment is funded mainly by earnings from export industries, converted into FRD savings. Therefore, export diversity is crucial to the long-term sustainability of investment.

While export diversification has progressed, Uzbekistan’s exports remain more concentrated and less sophisticated than those of other Asian countries. Figure 3.8.8 shows that, although the sophistication of Uzbekistan’s export basket has improved notably, it remains far less sophisticated than that of middle-income Asian countries such as Malaysia and the People’s Republic of China. The sophistication of Uzbekistan’s exports also lags behind the norm for countries with similar per capita income (Figure 3.8.9).

Uzbekistan’s export diversification is also very constricted (Figure 3.8.10), especially for sophisticated products in the core areas of metals, machineries, and chemicals. While the economy has expanded into somewhat more sophisticated products such as motor vehicles, they are still exported only to a few destinations, mostly to the Russian Federation. Uzbekistan therefore needs to expand its export markets for industrial products, as well as lift its product lines to those with higher value.

Policies and investments that improve the business environment, encourage private sector expansion, and strengthen infrastructure and logistics would promote a more diversified and sophisticated export sector. Uzbekistan is ranked last of 185 economies in the trading across borders category of the World Bank’s Doing Business 2013 report. Costs of exporting from and importing into the country average more than twice those of regional competitors. Liberalizing external trade through lower compliance costs, improved access to finance and foreign exchange, and simplified customs procedures would assist the private sector, which would in turn transform the economic landscape and promote growth. Structural reforms are especially important in view of continuing global uncertainty and the consequences for Uzbekistan’s export prospects of advancing regional trade integration, as evidenced by the recent customs union involving the Russian Federation, Belarus, and Kazakhstan.