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Research Report on Uzbekistan

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Main Economic Indicators of Uzbekistan

Macro indicators	2012	2013	2014
Gross gov. debt, bill UZS	8 274	9 910	12 256
Nominal GDP, bill UZS	96 723	119 750	144 868
Real GDP growth, %	8,2	8,0	8,1
Gross gov. debt/GDP,%	8,6	8,3	8,5
Deficit (surplus)/GDP,%	7,8	2,4	2,2
Inflation rate,%	10,4	10,2	9,8
Current account balance/GDP,%	-5,2	-4,3	-3,9

Development indicators	2014
Inequality adj. HDI	0,56
GDP per capita (Thou. of USD)	5,63

Sources: RAEX (Europe) calculations based on data from the IMF

Summary

Government debt metrics, foreign-currency reserves and fiscal position of Uzbekistan remain strong. The country has had stable GDP growth during the last decade. However, the overall level of economic development is still low with GDP (PPP) per capita at USD5600 in 2014. Uzbekistan imposes strict capital controls, has unfavorable investment climate and high levels of corruption. Official statistics is largely unreliable due to low level of transparency. Additionally, the country has no experience of peaceful power transfer since its independence in 1991.

External position deteriorated as a result of falling prices on Uzbekistan's export goods and devaluation of regional currencies that led to sharp drop in remittances from Russia. However, significant Central Bank reserves and regional diversification of exports will partly mitigate the difficulties.

Government debt and fiscal positions remain solid. As mentioned in our previous report[1] while total volume of gross government debt more than doubled over the last five years, main debt ratios remained strong at end-2014 (see graph 1). The Agency forecasts the volume of total government debt at 11,6% of GDP and 32,8% of budget revenues by end-2015.

Consolidated budget surplus[2] for 2014 was reassessed by IMF to a stronger 2,2% of GDP from the earlier figure of 1,7% (see graph 2). Fiscal balance showed a surplus in the 1H 2015 at UZS119bn (below 1% of 2014 GDP), but official projections suggest a deficit of 1% for 2015 driven by lower prices of export goods.

Capital controls is a highly negative factor. Policies of the Central Bank of Uzbekistan (CBU) aimed at controlling FX transactions as well as regulating exchange rates remain in place. These policies lead to black markets and other distortions. Recent devaluation of Russian ruble and Kazakh Tenge, combined with a reduction of net remittances from Russia (see graph 4) increased the gap between the official and unofficial exchange rates.

[1] http://raexpert.eu/reports/Research_report_Uzbekistan_06.11.2014.pdf
[2] Including Sovereign Fund for Reconstruction and Development.

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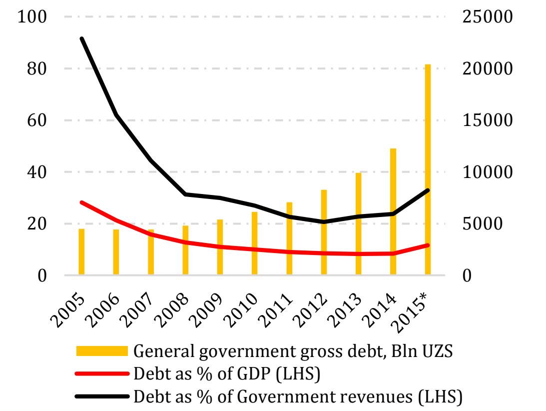
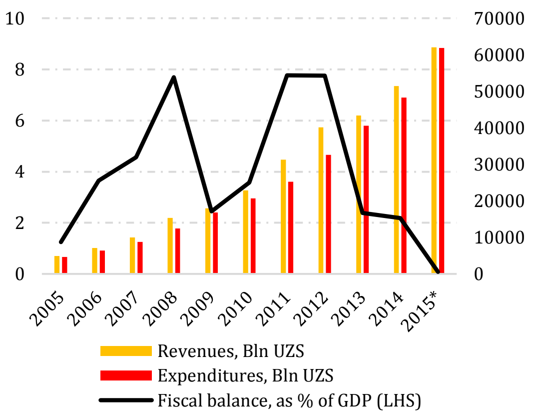
Graph 1: Uzbekistan's gross government debt



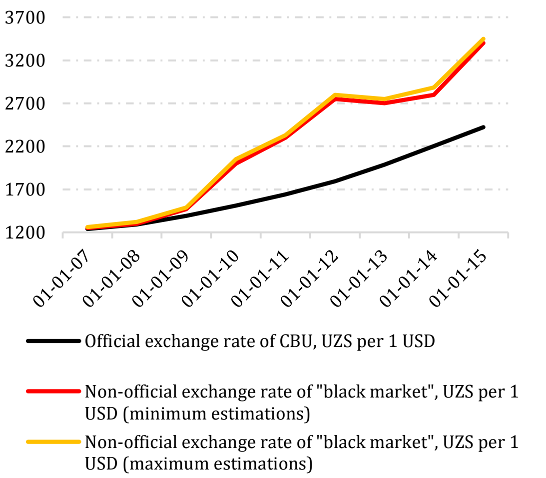
Source: RAEX (Europe) calculations based on data from the IMF
* IMF Estimations

Graph 2: Fiscal performance of Uzbek government



Source: RAEX (Europe) calculations based on data from the IMF
* IMF Estimations

Graph 3: Amount of UZS per 1 dollar in accordance of different exchange rates



Source: RAEX (Europe) estimates and the CBU

The Agency estimates this gap was about 40% at early 2015 (see graph 3), while media sources reported its rise to about 65% by mid-2015. Although the CBU widened the devaluation corridor of the UZS, the Agency expects the difference between official and unofficial exchange rate to exceed 50% by the end of 2015.

Regional slowdown and drop in commodity prices hit Uzbekistan. Current recession in Russia triggered a sharp drop in remittances to other CIS countries. The total amount fell by 40% during Q2 2015 compared with the same period of the previous year. Uzbekistan is the largest recipient of remittances from Russia among the CIS countries. Cross-border transfers of individuals from Russia to Uzbekistan dropped by more than 47% during Q2 2015 compared with the same period of the previous year (see graph 4).

Drop in global prices of Uzbekistan's main export goods (natural gas, gold and cotton) led to deterioration of current account balance of the country. However, compared with other CIS countries, Uzbekistan has lower dependence on Russia in terms of trade and importance of remittances. Less than 3% of exports and not more than 10% of imports come from Russia, while remittances from Russia were equivalent to about 12% of GDP in 2013 (compared to that of Tajikistan at above 40%). Additionally, Uzbekistan (as well as Turkmenistan) has long-term natural gas export contracts with China, which smoothens negative effects of price volatility.

State-coordinated investments partially compensate unfriendly business climate. Uzbekistan's real GDP growth remained one of the highest in the region at 8% in 2014 according to the IMF (see graph 5). Official figures for 1H 2015 also reported similar figures. These results were partly driven by high state investments in cooperation with foreign governments and companies. Major investments originate from Chinese state-owned companies mostly interested in the extraction sector and transport infrastructure. According to official statistics year-over-year growth of investments was 9,8% during the 1H 2015.

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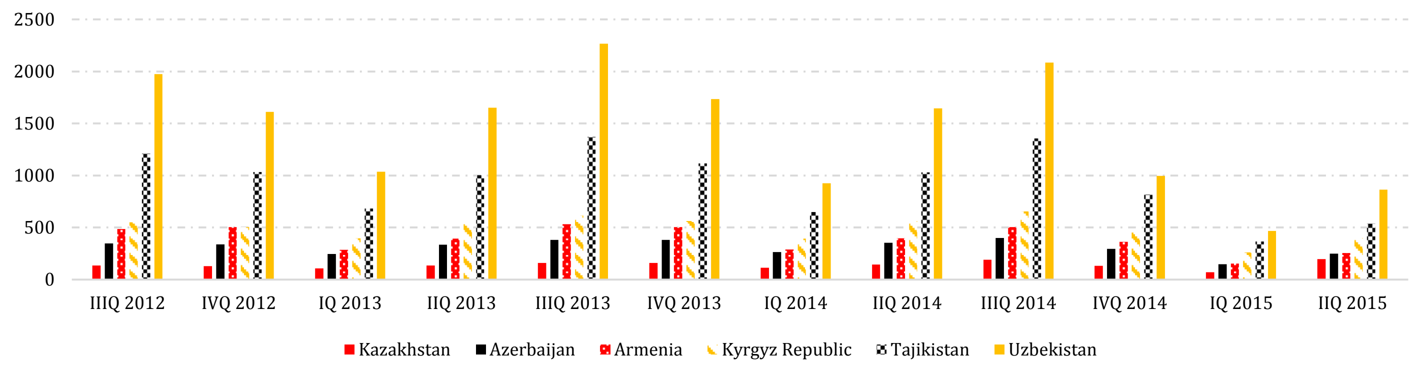
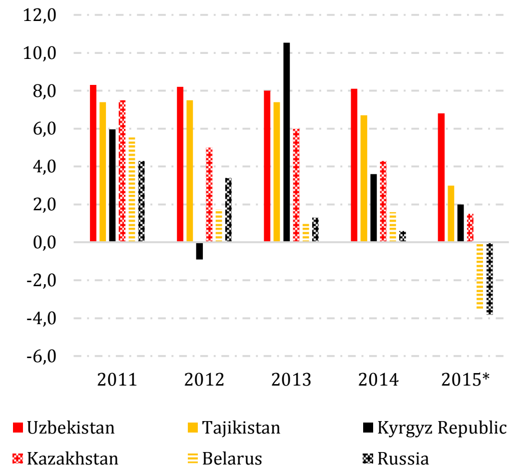
Graph 4: Cross-border transfers of Individuals, from Russia to CIS countries (Mln USD)



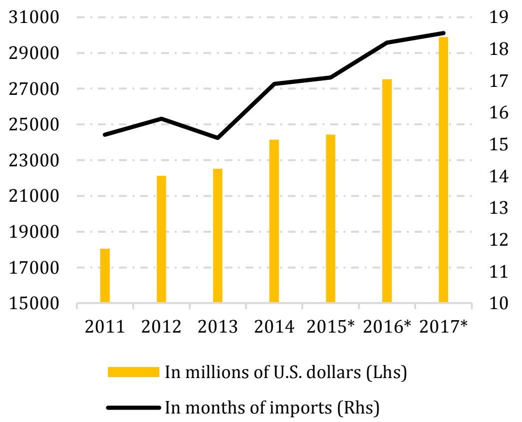
Source: RAEX (Europe) calculations based on data from the Central Bank of Russia

Graph 5: Real GDP growth for selected CIS countries



Source: RAEX (Europe) calculations based on data from the IMF
* IMF Estimations

Graph 6: Dynamic of gross official external reserves of Uzbekistan



Source: RAEX (Europe) calculations based on data from the IMF
* IMF Estimations.

CBU's policy led to significant reserves accumulation. Capital controls and obligations for exporters to surrender a large share of their FX revenues resulted in high accumulation of FX reserves at the CBU. According to latest assessment, reserves stood at USD24,1bn or 16,1 months of import at the end-2014. Reserves have increased by 30% since 2011 (see graph 6). This buffer allows the CBU to maintain capital controls and managed devaluation of the national currency in the medium term.

The CBU reduced the key rate from 10% to 9% in January 2015 to support economic growth and investment activity in the real economy. Inflation level reached single-digit figure in 2014, but 2015 inflation should exceed 10% driven by recently announced increase of utilities prices and the minimum wage.

Low level of institutional development remains key risk factor. Information transparency and reliability of official statistics in Uzbekistan remain among the lowest in the CIS countries. These factors make the overall assessment of the country very difficult. High levels of corruption, administrative economy and controversies associated with foreign investors reduce country's capacity to attract investors in industries outside the natural resources sector.

However, international financial organizations note significant improvements in institutional climate of Uzbekistan over the last year. Last IMF mission welcomed the authorities' announced strategy to strengthen corporate governance and accelerate privatization. Progress in structural reforms was also affirmed by current the WB's Doing Business rating that moved Uzbekistan to the 87th in 2015 from the 141th place in the previous ranking.

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