

Structural transformation in Uzbekistan Longer-term challenges for modernization

Uzbekistan has been always known, and often criticized, particularly in 90th, for its unconventional approach for economic reform. Unlike most of the countries of the region which were following so called Washington Consensus standard policy recommendations, Uzbekistan opted for a more gradual transformation of its economy. As a consequence, its GDP declined by only about 18% between 1991 and 1995 - a moderate reduction matched only by the richer transition economies of Central Europe. Moreover, government policies mitigated the impact of the economic downturn by instituting a decentralized form of social assistance, run by local communities - mahallas, which targeted income subsidies to the poorer sections of the population.

Beginning in 1996—when many other transition economies were still struggling with recession—Uzbekistan’s economy began to grow, and it averaged rates of over 4% from 1997 onwards. By 2001, its GDP had recovered to 103% of its 1989 level, making it the first former Soviet Republic to regain its pre-transition level.

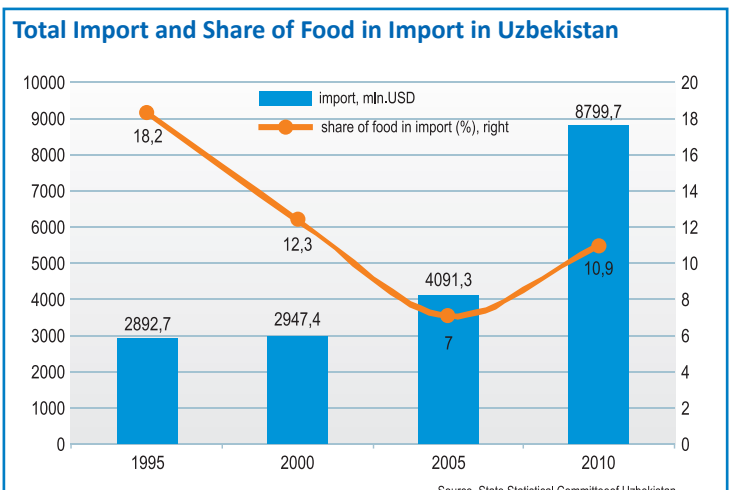
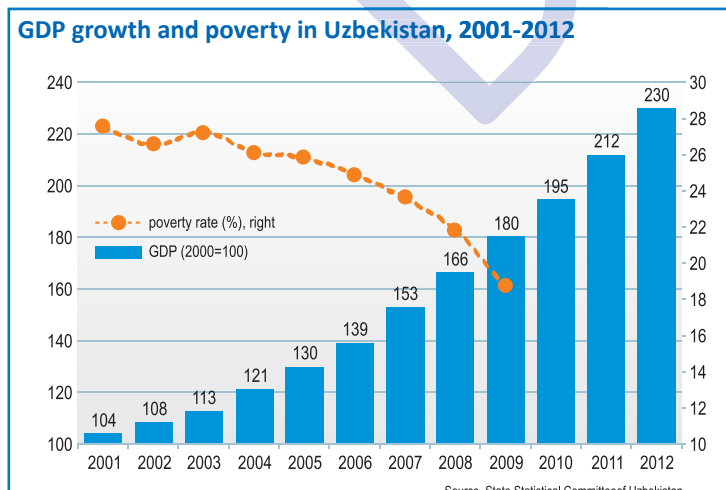
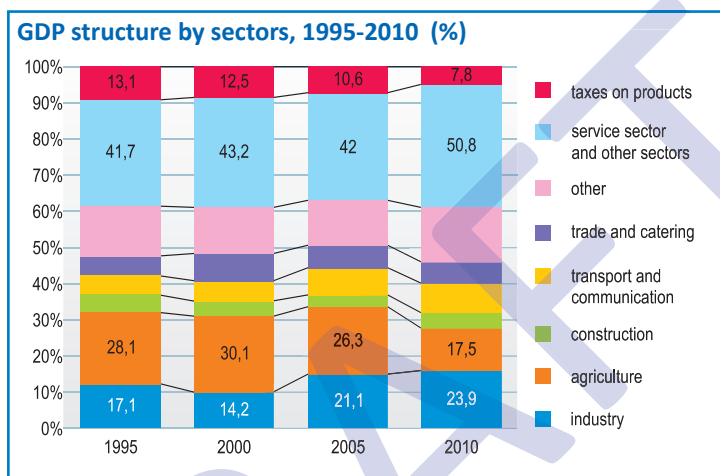
Early on, Uzbekistan also began to structurally transform its economy, adopting an import-substitution strategy and beginning to diversify out of its heavy reliance on cotton exports. By 2004 GDP growth accelerated to over 7% by 2004 and exceeded 9% in 2007 and 2008. This growth was based on rapid expansion of industry and fueled by increases in exports of commodities such as gold and gas. Domestic capital investment increased by more than 25% by 2007 and grew rapidly thereafter.

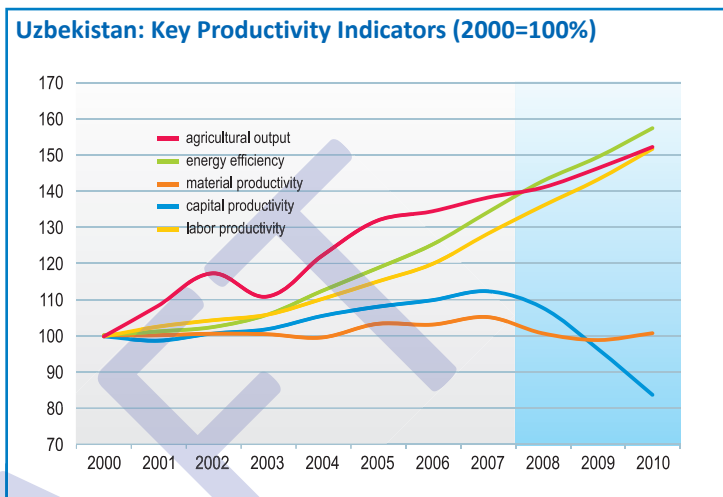
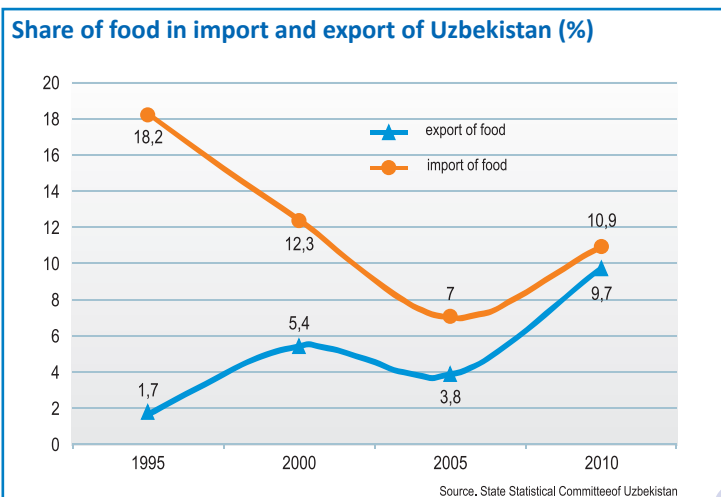
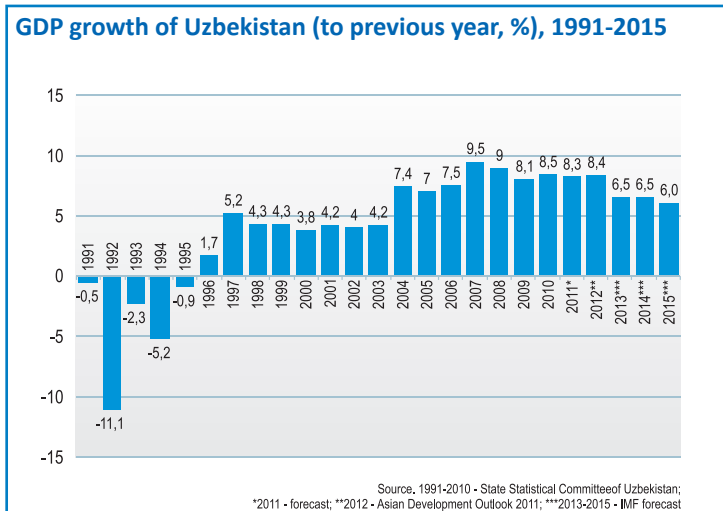
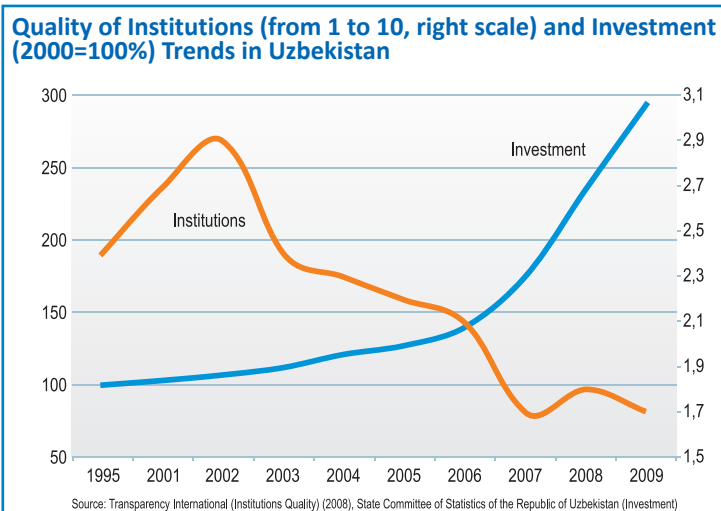
The Uzbek model is basically the model of a rapid industrialization and restructuring. Since mid 90th, Government has been concentrating resources and channeling those to “priority industries” associated both with import substitution and export promotion. This could not only secure self-sufficiency in such critical items as energy and food, and to avoid some of the worst effects of the food and energy crisis, and later the global financial crisis, but to accelerate growth in 2000th further and sustain. But more fundamentally, government managed to significantly increase the share of industry and services in GDP. For last several years Uzbekistan has been one of the world top performers in terms of economic growth, and projections for the coming decade look very positive.

Government also undertakes measures to ensure that this accelerated growth is transferred to poverty reduction, securing more egalitarian income distribution, particularly through higher social public expenditures.

The next stage of structural transformation during the years to come will be associated primarily with raising competitiveness on national industries. Reduced corporate and individual taxes, concessions for FDI, and access to resources from the Fund for Reconstruction and Development, as expected, will accelerate investment, which remains as a major means of this modernization program.

CER Policy Brief “Challenges of Modernization” (forthcoming in May 2011) outlines key challenges for the success of this ambitious investment program of the Government:





Prevalence of energy and transport in the structure of investment.

Directing most of investment to capital intensive industries restrains resources of growth in manufacturing and hi-tech industries. Moreover, since the priority sectors – particularly energy and transport – are capital – intensive, employment (and poverty reduction) has been lagging behind both the investment and economic growth. To improve these imbalances in some way, Government has announced earlier this year its plans to both accelerate structural adjustments and give more space for small and medium business.

Declining returns from investment. In 2000-2010 labor productivity increased by almost 150 %. Even more positive trend is in energy consumption. Growing world prices for oil and gas will keep incentives to further increasing energy efficiency high. Investment in new technologies will work for continuing growth in productivity. However the major concern is associated with the declining returns from investment. The reason for declining returns on investment can be a consequence of the development of capital-intensive industries and diminishing returns due to higher growth rates of capital compared with other factors of production. However, it would be critically important to evaluate whether these processes are natural or the result of inefficient use of capital.

Low Degree of Innovative Activity. Longer term sustainable economic growth cannot be provided without increasing entrepreneurial role of private sector open for innovations. Enabling environment for unleashed private sector would require not only reduced transaction costs, access to finance and better infrastructure. Government would need to play an increasing role in creating incentives for innovations, promoting R&D, investing in human capital, harmonizing reforms in

education (particularly in vocational and higher education) with its industrial policy agenda.

Lagging Institutional Transformation. While the volume of investment tripled from 2000 for 2009, the quality of institutions and public administration might become a major bottleneck for the ambitious modernization agenda. In November 2010 President Islam Karimov highlighted the importance of institutional reforms as part of further strengthening of democratic reforms and civil society. Transformation in Uzbekistan so far has been basically a “top-down” driven process. As the reform agenda becomes more complex and requiring longer term visioning, it will also involve an increasing number and variety of actors – both public and private - which need to become more mature. The major challenge ahead is to ensure that transformational processes involve effective bottom-up streams.

See also:

The Puzzling Success of Uzbekistan’s Heterodox Development

<http://www.soas.ac.uk/cdpr/publications/dv/file56073.pdf>

Industrial policy of the Republic of Uzbekistan: criteria to select priority sectors and products

<http://www.cer.uz/en/publications/978>

Family Assets Mobilization

<http://www.cer.uz/en/projects/271>

Urbanization and industrialization in Uzbekistan: challenges, problems and prospects

<http://www.cer.uz/en/publications/782>