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N E W S L E T T E R

U Z B E K I S T A N

Dynamic economic development in Uzbekistan

The Uzbek economy grew by robust 5.6% in 2019 on the back of high investment. For 2020, growth is expected to reach 6%.

Strong exports helped to decrease the current account deficit to 3.3% of GDP in 2019. At the same time, FDI increased to 1.8% of GDP and is thus mirroring reform efforts. FDI is expected to become an important source for financing the current account deficit in the future.

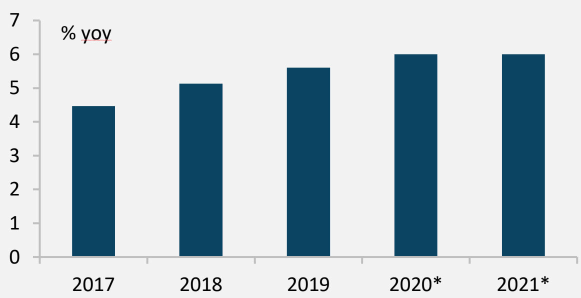
International reserves increased to high USD 29.2 bn by the end of 2019. The Sum's depreciation by 12% vs the US dollar in 2019 was driven by market forces. Inflation remained high in 2019 and increased to 15.2% in December 2019, also due to higher energy tariffs. Fiscal policy remains prudent: the budget deficit amounted to moderate 1.6% of GDP in 2019 and is expected to remain at this level in the coming years. Public debt equals 23.3% of GDP and is rather low by international comparison.

All in all, Uzbekistan shows robust investment-led growth with stable fiscal policy and increasing FDI. The government shows a remarkable pace at implementing economic reforms and plans to continue this course in coming years, including more complex reforms in the banking sector, privatisation and investment climate. The implementation of these reforms should give a further boost to the Uzbek economy.

Strong economic growth

The economy grew by 5.6% in 2019 and thus continues to develop dynamically. The growth drivers on the demand side are mainly investment, especially public investment, and private consumption. Investment increased by 46% in the first 9 months of 2019 compared to the same period of the previous year. Private consumption grew by 5.8% in this period.

Real GDP growth



*Source: IMF, *forecast*

In the sectoral perspective industry grew at 8.9% and thus faster than services at 5.1% and agriculture at 2.5%. The industrial sector accounted for 30% of GDP in 2019, while agriculture is responsible for 28% of GDP. The share of agriculture is large compared to other countries. As an example, Kazakhstan's agriculture accounts for 4.6% of GDP.

For 2020, growth is expected to reach 6%. Public investment is expected to grow more slowly due to planned reforms in the banking sector. Therefore, the focus should shift from public to private investment in the future.

High inflation

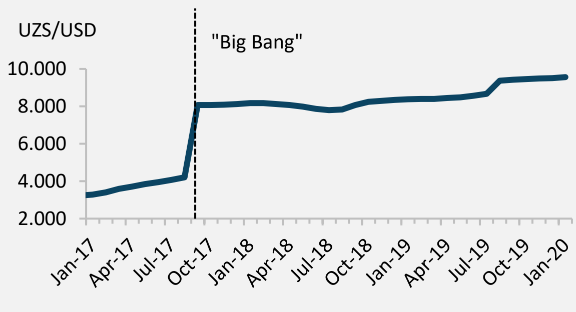
Inflation remained high in 2019. It increased to 15.2% in December 2019 from 13.0% in January 2019. The necessary hike of energy tariffs played an important role in this context. For 2020, a slight decline of inflation to 12.4% is expected.

The Central Bank raised the policy rate in 2017/18 from 9% to 16% in order to bring inflation under control. While this measure is already having some impact, inflation will probably only drop below 10% after 2020. The Central Bank plans to target a single-digit inflation rate from 2021 onwards.

External sector

After the liberalisation of the exchange rate in 2017, it is increasingly subject to market forces. However, the Central Bank is still closely involved by conducting currency interventions. In 2019, the Sum further devaluated by 12.3% vs the US dollar. This was driven by market forces such as rising foreign currency demand from Uzbek importers.

Exchange rate

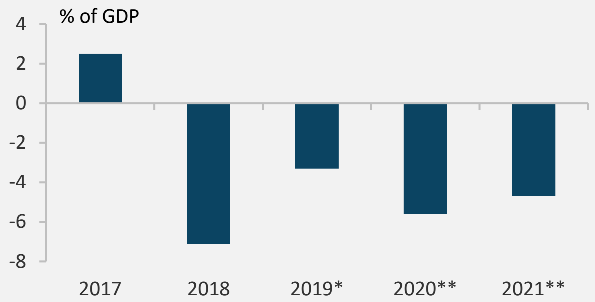


Source: Central Bank of Uzbekistan; end of month

At the same time, the international reserves of the Central Bank remain very high with USD 29.2 bn at the end of 2019. This is the equivalent to 13 months of import coverage.

The current account deficit of Uzbekistan narrowed to 3.3.% of GDP in 2019 according to preliminary estimates. This is low compared to 7.1% of GDP in 2018. This development was supported by strong growth of exports and of gold in particular. Even if not permanent, the reduction of the current account deficit is a positive development. In 2020, the deficit is expected to rise again, due to an expansion of domestic demand and imports.

Current account balance



*Source: World Bank; *own estimation based on 9M2019;*

***forecast World Bank*

An important factor to finance the current account deficit are FDI inflows. FDI has been increasing since 2018 and amounted to 1.8% of GDP in 2019, as estimated by the World Bank. In 2020, FDI is forecast to amount to 2.1% of GDP, which is positive and reflects reform efforts.

Foreign trade is also rising strongly. In the first 11 months of 2019, exports increased by 53.4%, while imports rose by 29.4%. This expansion of foreign trade is remarkable, taking into account a difficult global environment.

Fiscal policy remains prudent

In 2019, the budget deficit amounted to moderate 1.6% of GDP. This figure refers to a broad deficit definition and takes into account quasi-fiscal activities of the government. Public debt was around 23% of GDP at the end of 2019 and thus very low by international comparison. In 2020, the deficit is expected to slightly increase to 1.8% of GDP, while public debt should increase to 25% of GDP. These relatively low deficits and debt level show the continuation of the prudent fiscal policy.

Outlook

Uzbekistan's economy has developed very dynamically since the beginning of the reforms in 2017. This development was characterised by exchange rate flexibility, a strong increase in foreign trade, rising investment, higher FDI, but also significant inflation. It is very positive that fiscal policy remained prudent. Additionally, high international reserves provide a comfortable buffer against possible external shocks.

After a considerable reform progress has been achieved and low-hanging fruits have been picked, more difficult reforms have to be tackled. This includes banking sector reforms, the privatisation of state-owned enterprises and streamlining the regulatory environment. Implementing these reforms should give a further boost to the Uzbek economy and make Uzbekistan more attractive for international investors.

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