

## Impact of COVID-19 on the Uzbek economy

The Uzbek economy is projected to grow by 1.5% in 2020 - before the COVID-19 crisis, an increase of 6% had been expected. The lower figure results from lower growth in consumption and investment as well as in services and industry. Agriculture is almost unaffected by the crisis.

Exports and imports will fall significantly in 2020; gold exports, on the other hand, will continue to rise strongly. The current account deficit will reach 9.6% of GDP, a high figure, which, in addition to the decline in exports, is caused by lower remittances. Despite very high reserves of USD 31.3 bn, financing the deficit by IFIs is recommended.

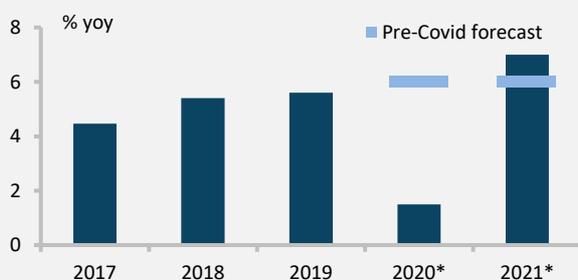
Inflation is set to reach 12.9% and thus be slightly lower than expected before the pandemic. The Sum depreciated slightly by 6% vs the US dollar in Jan-May. The budget deficit will rise to a relatively high 5.6% of GDP in 2020 due to higher spending and lower revenues. International donors are expected to finance a large part of the deficit. The debt level is expected to reach 34.5% of GDP, thus remaining moderate despite the high deficit.

All in all, the Uzbek economy will grow despite the pandemic and is therefore in a better position than most other countries. For 2021 strong economic growth of 7% is forecast.

### Growth declines sharply, but remains positive

In response to the pandemic, Uzbekistan has taken very strict containment measures, which were implemented relatively early. The number of infections was kept low (5,730 confirmed cases; as of 18 June 2020), but the measures had a negative impact on the economy.

#### Real GDP growth



Source: IMF, \*forecast

In 2020, GDP is expected to increase by only 1.5%, compared to 6.0% forecast before the pandemic. The reason for the decline is lower growth of individual GDP components. Private consumption is expected to grow by only 0.3%; investments by only 4.5%. On the other

hand, a strong increase in government spending by 12.7% is assumed, which should strengthen the economy.

This development is mirrored on the supply side. Industry is expected to grow by only 2.1%, while the service sector is expected to grow by only 0.6%. Agriculture, on the other hand, will have a stabilising effect. It accounts for 28% of GDP, a very large share, and its growth forecast remains unchanged at 2.6% despite the pandemic.

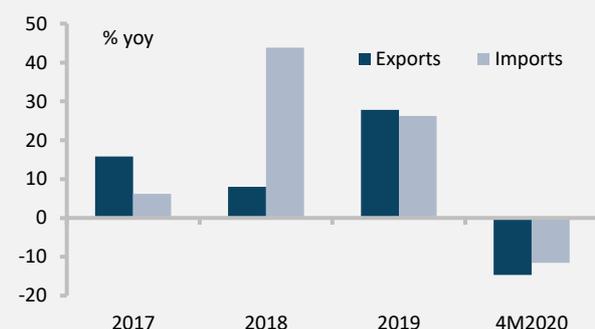
### Slight decline in inflation

Inflation is expected to reach 12.9% in 2020 - a slight decrease from the original forecast. The main reason lies in the lower aggregate demand. The central bank reacted by slightly lowering the policy rate by one percentage point to 15% in April 2020 and is sticking to its target of reducing inflation gradually to 5% p.a. by the end of 2023.

### Decline in external trade

After strong growth last year, external trade is expected to shrink in 2020. Imports fell by 12% in the first four months, exports by 15% yoy. The decline in exports can be observed in almost all commodity groups, e.g. natural gas exports fell by 51%, textile fibres by 54% and fruit and vegetables by 35%. In contrast, exports of gold rose strongly by 27%.

#### External trade



Source: State Committee on Statistics

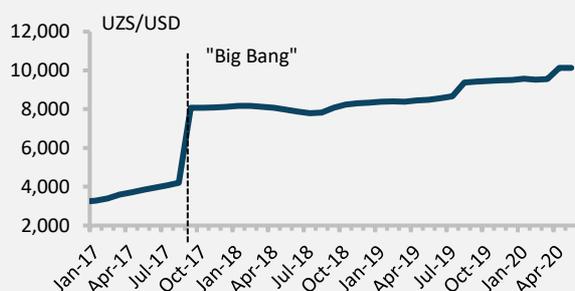
The share of the EU in the Uzbek goods exports is about 1% and thus still very small. However, with the prospect of GSP+ preferences and the associated duty-free market access for many Uzbek products – including textiles – this share should increase in the medium-term.

### Slight depreciation of the Sum

The Sum depreciated by about 6% vs. the US-Dollar in the period from January to May 2020. This weakening

is linked to declining exports and remittances. According to the central bank, remittances in April 2020 were 50% lower than in April 2019, which reduces the supply of foreign exchange. The exchange rate floats relatively freely and the central bank intervenes only to smooth fluctuations and to offset sales of gold.

#### Exchange rate



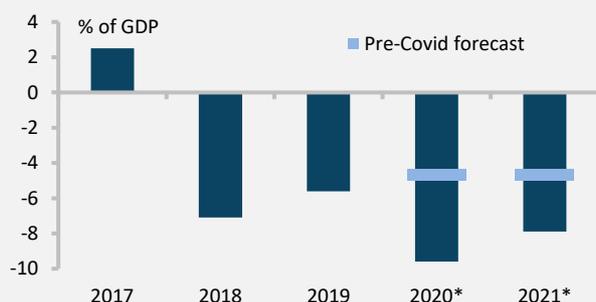
Source: Central Bank of Uzbekistan; end of month data

The slight depreciation is appropriate in the light of high inflation.

#### Doubling of the current account deficit

The current account deficit is expected to rise to high 9.6% of GDP in 2020. This development is also attributable to the decline of exports and remittances. Theoretically, the deficit could be covered by high international reserves. In May, these stood at USD 31.3 bn, which corresponds to an import coverage of about 14 months - a very high figure. On the other hand, the use of reserves alone would undermine confidence. To finance the deficit, the government is making use of international support, e.g. the IMF has already granted loans.

#### Current account balance



Source: IMF, \*forecast

#### Strong increase of the budget deficit

The budget deficit is expected to rise to 5.6% of GDP as a result of the COVID-19 crisis. The reasons are declining revenues on the one hand and rising expenditure to support the economy and the population on the other. Despite the high deficit, debt is expected to reach only a moderate 34.5% of GDP in 2020. In our view, the temporary widening of the deficit

is not a threat to financial stability. The measures taken to support the population and businesses are justified.

However, financing the deficit requires the support of IFIs, as the domestic market is too small. The government has set a target to receive international assistance of USD 1.6 to 3.1 bn until August, which would correspond to about 2.6% to 5.0% of GDP. This target is not unrealistic.

#### Conclusion and outlook

The Uzbek economy was hit hard by the COVID-19 crisis. Compared to other countries, however, the decline in the projected growth of 4.5 percentage points is moderate. The reasons lie in the fact that the crisis is hitting a rapidly growing economy and the infection numbers are low. Uzbekistan also has the advantage of having spent its resources wisely, and now has large currency reserves and a low debt level as a buffer.

In 2021, growth is expected to accelerate again to 7%, which can be described as a "V" shaped recovery. There are already positive signals: a reversal of the trend in remittances seems to have already taken place in April and direct investment is also developing much better than expected, according to Uzbek sources. In the medium term, we see especially in agriculture a large development and growth potential, which could boost the overall economic development. However, this would require continuing the already initiated reforms towards market economy principles and undertaking the necessary investments.

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This newsletter is based on the 3rd issue of our [Economic Monitor Uzbekistan](#).

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