Event Report

EIAS European Institute for Asian Studies

Uzbekistan: Advancing Reforms for Investment and Regional Cooperation

EIAS Briefing Seminar
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Abstract

On 12 February 2020, the European Institute for Asian Studies (EIAS) in cooperation with the Embassy of Uzbekistan hosted a briefing seminar titled "Uzbekistan: Advancing Reforms for Investment and Regional Cooperation". The seminar was divided into two sessions moderated respectively by EIAS Senior Associate Mr Erik Famaey and EIAS Programme Director Mr Alberto Turkstra. The panel discussion brought together European and Uzbek officials and experts, representing the energy, finance, trade and infrastructure sectors. The first panel discussed the 2020 Tashkent International Investment Forum, while the second panel focused on the potential for EU-Uzbekistan regional economic cooperation in Central Asia, and Uzbekistan's aspired membership of the World Trade Organization and cooperation with the Eurasian Economic Union (EAEU).

1. The 2020 Tashkent International Investment Forum

The event began with a welcome speech by EIAS CEO Mr Axel Goethals. Mr Goethals introduced Uzbekistan as a fast-developing country, nominated "country of the year" by The Economist in 2019, due to its rapid economic progress.

The opening remarks were continued by H.E. Mr Dilyor Khakimov, Ambassador of Uzbekistan to the Benelux countries and the European Union. He stated that, in the last three years, Uzbekistan has been implementing very ambitious reforms which are proving to be successful. For this reason, the 2020 Tashkent International Investment Forum will further support the realisation of Uzbekistan's new growth agenda, attracting foreign investors. H.E. Mr Khakimov also emphasised the importance of this seminar for the further deepening of understanding of Uzbek foreign direct investments projects and privatisation measures.

The floor was then passed on to EIAS Senior Associate Mr Erik Famaey, moderator of this first panel, adding that Uzbekistan is opening up at a time when other countries are in retreat and that the Uzbek economy has been benefitting from this global adjustment. In fact, the Uzbek economy is expected to grow by about 6% per annum, surpassing other emerging markets such as China and India. Mr Famaey also explained that Uzbekistan has now momentum as well as structural advantages such as a demographic dividend, along with being the most populous in Central Asia.

Mr Famaey also mentioned that the current common perception attributes China's Belt and Road Initiative (BRI) to support the rise of Central Asia. Although this initiative will boost Central Asian economies, it is the ability of these emerging markets to attract foreign direct investments (FDIs) from all over the world, as well as their capacity to provide with a fair, level playing field and platform for investors to operate in the market, that will serve as the economic catalyst for Uzbekistan. Hence, it is the "spectacular, ambitious and bold" reforms in Uzbekistan that are attracting FDI rather than them being a consequence of the BRI.

The first panel discussion addressing the 2020 Tashkent International Investment Forum was then inaugurated by Mr Oybek Shaykhov, General Secretary of the Europe-Uzbekistan Association for Economic Cooperation. Mr Shaykhov emphasised the need for enhanced dialogue between European and Uzbek companies. In fact, European companies lack information about the Uzbek market's developments and find themselves at a disadvantage compared to Russian, Chinese, Korean and Turkish companies that have so far had the upper hand in terms of communication and information technologies. Consequently, the main mission is to establish effective dialogue among companies. He then concluded by stating that the Tashkent International Forum will be the first attempt of the country in actively playing a greater role on the international scene.

The second speaker of this panel was Mr Marat Terterov, the Head of Unit for Expansion at Energy Charter. He added to the discussion with an *excursus* into the very first economic reforms implemented at the end of the 1990s which led to different outcomes compared to the latest reforms. Although the Uzbek government at that time reflected the same interests of Mirziyoyev– to engage the world and attract FDI– the economic environment was marked by sectoral monopolies and concrete restrictions on trade, investments and freedom of currency exchanges. Consequently, despite the country receiving FDIs, engaging the world and implementing new policies, there are some substantial differences with the current reforms.
In fact, the region is starting to resemble the European Union (EU) in terms of freedom of movement of goods, services and people, as well as open borders. As a result, perceptions of

political opening in terms of regional and global cooperation have improved as the environment has become part of a more dynamic space. New aspects of policy and legislation have been enacted as well. In addition, the level of bureaucracy has been reduced and government decision-making has become more fluid and experienced due to a new generation of young policy makers who are more prone to interact with foreign investors and consult with international advisors.

Mr Terterov also explained how Uzbekistan's geographic partnerships are evolving. Since the early days of independence, Russia was the main "other" and trade partner for all ex-Soviet states. However, today China seems to be replacing Russia. Especially taking into consideration that it has more registered companies in Uzbekistan than any other foreign nation. The EU is also emerging as a relevant partner. Indeed, European companies could play a substantial role in the future, in particular in the solar energy sector, as a result of the shift of the economic environment from sectoral monopolies to free competition where investments are effectively protected by a legal security framework provided by the Energy Charter Treaty.

Lastly, Mr Terterov stated that many challenges await Uzbekistan in the future. In fact, despite the great progress made in terms of liberalisation so far, unlocking private equity and directing it into the country represent the next challenges to be tackled.

Mr William Flemming, Senior Adviser of Qantara Capital, was the third panellist. As an investment banker, Mr Flemming's intervention provided insights on the Uzbek banking sector. He stated that Uzbekistan offers many opportunities for investors. Nevertheless, there is still a low penetration rate of banking sectors services, especially in relation to retail and real estate banking. At the end of 2019, Uzbek banks' total assets amounted to USD 30 billion, equalling to 50% of its GDP. However, the small dimensions of the financial market are apparent when compared to the Belgian bank KBC's total portfolio assets. In fact, Uzbekistan's total banking loans amount to 10% of KBC's overall portfolio assets. Hence, it makes up of a small sector, albeit rapidly growing. Indeed, banking assets have tripled in the last few years, affirming Uzbekistan's economic development. Mr Flemming explained that this increase in assets is partly due to the devaluation of the *so'm* –the Uzbek currency– and that the assets will remain stable for the next 24 months. Overall, the banking sector is well capitalised, despite its low profitability for the largest state-owned banks due to state directives and policies.

Consequently, the banking sector will have to tackle some major challenges in the future such as the very high interest rates (caused by the high levels of inflation that have been permeating the economy since 2017), as well as the lack of trust towards the banks. In fact, Uzbek banks capture only 10% of savings, which mainly originate from the government, whereas 80% of the household savings "are kept hidden under the mattresses". Additionally, state-owned banks continue to dominate the scene since privately-owned banks make up for only 13% of the sector whilst less than 3% of the banks are owned by foreigners.

Mr Flemming also mentioned that the comprehensive reforms enacted by the Mirziyoyev administration are privatizing state-owned banks. In April 2019, the three major Uzbek state-owned banks were fully commercialised whilst the privatization process is gradually taking place for the rest of the banks.

Foreign investments in the banking sector are contributing to fill the existing gap with the private sector, thereby helping to mitigate political risks. Mr Flemming concluded by stating that more reforms are still needed to privatise the banking sector. He also emphasised the importance of

offering investors a fair, level playing field, transparency, disclosure of information and regulatory frameworks.

The moderator then introduced the final panellist, Mr Peter van der Veeken, Managing Director of CJ ICM Logistics. Mr van der Veeken's concise intervention highlighted the importance of communication routes for landlocked countries. In the case of Uzbekistan, developing efficient infrastructure facilities appears to be vital, also considering that the country's strategic location in Central Asia for accessing Kazakhstan, Turkmenistan, Kyrgyzstan as well as Tajikistan.

Mr Famaey concluded this first session with a question to the panel addressing the comparative advantages of Uzbekistan. Mr Terterov and Mr Shakov jointly responded. While Kazakhstan was previously the primary player in the banking and financial markets in Central Asia, today, Uzbekistan offers "hidden gems" in those same sectors. In fact, little explanation is given about the way European companies might access the Uzbek market whilst markets such as the Ukrainian or the Polish are saturated with information. Mr Shakov then continued by observing that until recently Uzbekistan was a closed economy. In only three years time, not only has Uzbekistan's economic environment become more dynamic and rich of potential, it has also started to find its way into the world economy.

2. <u>EU-Uzbekistan: Potentials for regional economic cooperation in Central Asia</u>

The second panel was moderated by EIAS Programme Director, Mr Alberto Turkstra, who introduced the topics of this session: the potentials for EU-Uzbekistan regional economic cooperation in Central Asia; cooperation between Uzbekistan and the Eurasian Economic Union (EAEU) and potential membership; as well as Uzbekistan's entry into the World Trade Organization.

The first speaker was Mr Pierre Emmanuel Thomann, Director of Eurocontinent. Mr Thomann initiated the debate with an analysis of the current geopolitical assets of the Eurasian continent. Brexit has fragmented the European project, while the EU has also been disconnected from Eurasia due to its chasm with Russia over the illegal annexation of Crimea. Mr Thomann proposed a new geopolitical asset that envisages Europe as a pivot to Eurasia. He recommended the EU to negotiate a new security architecture with Eurasia, Russia and China to increase profits and move beyond being perceived as a "sub-element of the Euro-Atlantic" alliance, impeding cooperation between the EU and Eurasia. As the world is increasingly endorsing multipolarity, the EU should start negotiations with China and grasp the opportunities offered by the BRI in Central Asia, while also resolving its divergences with Russia "to avoid an American-Chinese dominion". Implementing this Eurasian security architecture will prove to be complex but fundamental for the achievement of a better balance of power in the region. As a result, the EU should become bolder at the geopolitical level and endorse a more polycentric approach. Mr Thomann concluded by stating that supporting enhanced cooperation among Central Asian countries is the key to success for this strategy.

The moderator then offered the floor to Mr Ravshan Mamatov, Deputy Chief of Mission of Uzbekistan to the Benelux countries and the European Union. Mr Mamatov tackled the issue of cooperation between Uzbekistan and the Eurasian Economic Union focusing on the motivations for Uzbekistan to establish a partnership with the member states of the EAEU. Uzbekistan's foreign policy has been fostering regional dialogue to increase exports, attract investments and import resources by significantly reducing trade barriers and customs duties. Since Uzbekistan started

promoting an open dialogue approach with its neighbours based on equality, mutual benefit and respect, trade has almost doubled. He explained that Uzbekistan disapproves of initiating dialogue with a country by restricting cooperation with others. The Union represents a promising market for Uzbekistan and by reducing bureaucracy levels trade exchanges will be facilitated. Considering that a rising number of Uzbeks reside and engage in labour activities in the countries of the EAEU, the Uzbek government is contemplating cooperation with the bloc due to its labour market necessities, and to improve the life quality of its citizens. Additionally, as a transit corridor country, Uzbekistan provides the shortest route to the EU which would result in a significant reduction of transportation costs.

Lastly, he mentioned the great benefits that enhanced cooperation will bring to science and education. Mr Mamatov also reaffirmed that, although the debate on whether Uzbekistan should enter the EAEU as a member state or as an observer is continuing, joining an international organization will not prevent the country from establishing cooperation with other international organizations.

The third speaker of the panel was Mr Jocelyn Guitton, Policy Coordinator for Central Asia and Russia of the Directorate General for Trade of the European Commission. He addressed the issue of enhanced trade cooperation between the EU and Uzbekistan. He stated that the EU strongly supports regional economic integration and cooperation among Central Asian countries as it is a region characterized by a broad diversity of trade models akin to the European Union. In fact, some Central Asian countries engage in trade institutional relations with the EU and the EAEU whilst others are either members of the World Trade Organization or beneficiaries of the Generalised Scheme of Preferences (GSP). Currently, the EU is negotiating non-preferential agreements with Uzbekistan, Kyrgyzstan and Azerbaijan as they meet the GSP requirements for unilateral access to the EU market as low-income countries.

As for trade relations between the EU and Uzbekistan, statistics place the EU as Uzbekistan's third trading partner. According to Mr Guitton, this represents an anomaly as the EU has a trade surplus and usually ranks second or first in developing countries' trade lists. Nevertheless, there is great potential to enhance cooperation between the EU and Uzbekistan. In fact, in November 2018, negotiations for a comprehensive agreement, the Enhanced Partnership and Cooperation Agreement (EPCA), formally began in Brussels. The aim is to increase trade and investments and to promote European international rules and standards in Uzbekistan. The next round of negotiations will take place in Tashkent in March 2020.

Mr Guitton also mentioned that the challenges to the negotiation process reside in Uzbekistan not being a member of the WTO. Negotiations for its WTO entry have been progressing for the past fourteen years. Furthermore, in parallel with the EPCA agreement, Uzbekistan has also expressed interest in joining the GSP+ system. Since these memberships are fully compatible with each other, the EU is providing technical assistance to Uzbekistan to join both the WTO and the GSP+ system.

Mr Maciej Madalinski, Cooperation Officer for Uzbekistan of the European Commission's Directorate-General for International Cooperation and Development, concluded the second panel's discussion with his intervention regarding Uzbekistan's entry into the WTO. He began by stating that, following the new EU Strategy on Central Asia launched in 2019, the EU supports regional connectivity and prosperity within the region and is zealous about facilitating Uzbekistan's WTO

accession. In fact, the EU aims to contribute to Uzbekistan's economic development by aiding the government in creating a trade environment that conforms to WTO rules.

Mr Madalinski continued that the EU seeks to enhance both the Uzbek government's and people's understanding of its WTO accession; raise stakeholder and private sector awareness of the WTO proceedings; strengthen national capacities for sanitary and phytosanitary measures, technical barriers to trade and trade facilitation compliance; support the government in fulfilling WTO Accession Requirements, and in reforming national trade policies. He concluded by offering some examples of how the European Union is assisting Uzbekistan. Indeed, between September 2019 and February 2020, the European Commission's International Trade Centre has engaged in training workshops on Trade in Services and Domestic Support in Agriculture, as well as in organizing roundtables and offering provisions of technical support for the preparation of documents related to the Accession process.

The panel concluded with a Q&A session. A question was raised on the dynamics for integration in Central Asia considering that the region is comprised of five different countries with different stances on the meaning of the concept of "community" that could potentially be created among them. Mr Thomann addressed the question by explaining that the current integration process in Central Asia excludes the political dimension. The rationale behind it is motivated by the need to avoid division caused by the great powers operating in the region.

Mr Mamatov also contributed to the remarks by adding that there already existed a similar initiative, which was replaced by bigger organizations such as the EAEU. However, in the last two years, a new format has appeared in the form of informal meetings between the Central Asian heads of state, principally solving economic issues. President Mirziyoyev initiated the trend, of which the latest meeting was held in Tashkent last year. Nevertheless, it cannot yet be predicted whether this will lead to the creation of a new official organisation, to assist with the next stages of integration. But at the very least, it contributes to growing trust between the Central Asian republics.

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