

Improving trade policy for human development

United Nations Development Programme

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Introduction

During recent years increasing exports were one of the key factors in maintaining high economic development rates in the Republic of Uzbekistan: Average annual growth in exports during 2004–2008 was 25.3 percent, while GDP grew on average at 8.1 percent per annum.

However, high economic growth rates do not automatically lead to improved public welfare. According to the human development concept, improving the qualitative parameters of human life (public access to basic healthcare and education services), distribution of income (evenness of distribution, share of low-income category), guaranteeing fundamental human freedoms and rights, and providing each person with choices throughout all aspects of life, are equally important. Taken together, along with the level of real income per capita, these factors portray the real welfare of people living in a given country.

If all of the aforementioned factors are taken into account, it must be noted that the high economic growth rate observed in Uzbekistan for a number of years, was accompanied by less dynamic improvement in many parameters of human development. In particular, the poverty reduction rate was relatively slow¹, while elasticity of employment versus GDP growth rate was only 0,21².

An important factor in achieving sustainable long-term economic growth along with considerable improvement in human development indices can be a restructuring of the economy, aiming to reduce the share of commodities in total output and exports of the country. A low share of finished products with high value addition in the total volume of exports does not only impede the growth of real income, but also increases the sensitivity of the country's macroeconomic position and public welfare to unstable global commodities markets, which could adversely affect the human development indices.

In such circumstances, an evaluation of Uzbekistan's trade policy in terms of its efficiency with regard to human development is timely. In this context, the main goal of this research is to analyze how foreign trade policy impacts of human development and to determine the main directions for improving the former with a view to achieving improvements in human development indices.

To achieve this goal, the following tasks need to be undertaken:

- analysis and summary of international experiences in terms of the trade policy's effect on human development;
- analysis of the effect of Uzbekistan's trade policy on human development, at each stage of reforms;
- analysis of the impact of the global financial and economic crisis on the main macroeconomic indices and human development in Uzbekistan;

¹ According to estimates, elasticity of poverty level versus economic growth in Uzbekistan is 0.32. See McKinley, Terry, Weeks, John, A Proposed Strategy for Growth, Employment and Poverty Reduction in Uzbekistan. Country Study No. 12, October 2007.

² Calculations were made based on data on GDP growth and employment rates for 2000–2007.

The goal of the research is to analyze the impact of trade policy on human development

– determine the main directions for improving trade policies to ensure human development post-crisis.

While conducting the research, methods of comparative and statistical analysis were used. The research resource database includes current regulatory and legal acts of the Republic of Uzbekistan, data of the State Statistics Committee of the Republic of Uzbekistan, Ministry of Economy of the Republic of Uzbekistan, and scientific research materials.

The results of this research can be used by state authorities in the process of improving trade policies with a view to ensuring human development in the Republic of Uzbekistan.

Chapter 1. Foreign Trade and Human Development: Analysis of International Experiences

The relationship between foreign trade and human development is complex and controversial.

The growth in foreign trade and changes in its structure may contribute to increased economic productivity through deeper specialization and scale, access to new technologies, dissemination of new knowledge, and development of competition. All of these directly impact upon the economic growth rate and increase employment and household incomes. In turn, additional income generated in such a way can be used to improve the quality of life and expand the possibilities and capacities of a human being, including improving health, nutrition, quality of education and skills.

As one of the central components of the human development concept is providing each person with freedom of choice, it is important to note that foreign trade may significantly expand choices for people through increased assortment of goods in the domestic market, as well as through opportunities to sell goods and services in new markets. In addition, increased production and sales of goods, the production of which requires higher qualifications, will increase the demand for a highly-skilled workforce and create incentives for improving the quality of the workforce and the general level of education in the country.

However, rapid liberalization of foreign trade in a country where the majority of manufacturers are unable to produce goods that would be competitive in an open economy, could cause a number of enterprises to curtail their operations, with a subsequent growth in unemployment, reduced household incomes and an ensuing reduction in the human development indices in the short term.

Hence, the question arises, which trade regime creates the most favourable conditions for achieving sustainable high economic growth and human development rates; and what should be a country's strategy to realize the potential of its trade policy as a factor in human development.

In the majority of cases, with the development of a country's economy, its trade regime becomes more liberal, and researchers frequently propose accelerated liberalization of trade policy in order to achieve sustainable growth and development in the longer term.

There are a number of examples, which suggest that rapid liberalization of foreign trade does not guarantee acceleration in economic growth rates, nor does it secure higher human development. For example, the large-scale liberalization of Haiti's foreign trade policies during 1994–1995 – when import tariffs were significantly reduced, with the ceiling set at 15 percent and all quantitative limitations were also abolished – resulted in the economy stagnating and the population's welfare worsening, with a subsequent negative impact on the human development potential of the country.

Moreover, there are further examples of high economic growth and human

The relationship between foreign trade and human development is rather controversial

development rates being achieved with a relatively low level of openness in the national economy. For instance, in the mid-1980s, Vietnam exercised a state trade system, maintained the state monopoly on import operations, and applied high tariff and non-tariff barriers with respect to agricultural and industrial imports. At the same time, the country carried out deep institutional reforms targeting the liberalization of the domestic economy. The result of such reforms was not just considerable improvement of economic indices (by the end of the 1980s annual economic growth rates were on average 8 percent, foreign trade was growing at high rates, and investment was flowing into the country), but also significant improvement in public welfare and a substantial decrease in poverty.

These two examples demonstrate that rapid liberalization of foreign trade policies is not sufficient for accelerating economic growth rates, reducing poverty and improving the country's public welfare. In order to achieve high human development results, trade policies should take into account the level and the nature of the country's economic development. Foreign trade reforms should be preceded by institutional reforms allowing a reduction in domestic barriers for economic development. Primarily, these include the barriers that limit the freedom of entrepreneurship and competition, as well as inefficiency of public services. Trade liberalization in a country with low opportunities for the private sector to realize the benefits arising as a result of such liberalization, will most likely not allow the domestic economy to efficiently integrate into the global economic framework, and may also create a multitude of additional economic and social problems.

For countries with a relatively low level of development and undeveloped market institutions, liberalization of foreign trade is more a second step in economic reform. The first step would involve creation of domestic potential, allowing the national economy to benefit from opportunities emerging from foreign trade liberalization. With such an approach, foreign trade liberalization is seen not as the main cause of accelerated economic growth, but as (i) the result of such acceleration; and (ii) an important condition for ensuring sustainable economic growth.

It is not a coincidence that countries experiencing high economic growth rates over the past decades had a significant reduction in their trade barriers. For instance, in China and India, which are often highlighted as countries that achieved impressive economic results through open foreign economic policies, large-scale foreign trade liberalization only occurred once radical internal reforms had been implemented. However, in China, the economic development originated in the 1970s, while trade regime liberalization measures only started in the mid-1980s. India has been experiencing significant economic growth since the 1980s, while trade liberalization measures only started in the early 1990s³.

Foreign experience also indicates that it is appropriate to establish the principles of trade policies based on the priorities of the country's overall development strategy. For instance, trade policies aiming to implement the national development strategies and accompanied by a series of reforms in

³ India's and China's experiences have to be viewed with caution, given the immense size of their economies. Large-scale domestic economies allow for acceptable levels of competition and economies of scale, even if they are mostly closed.

Trade policies should take into account the level of the country's economic development

other areas, are the main cause of the considerable acceleration of economic development rates in East Asian countries, and them becoming known as “Asian tigers” and “Asian dragons”. Besides the export stimulation measures, these countries took measures to stimulate savings and investments, diversify the economy, protect domestic markets, and increase educational levels. Although many of these measures largely deviated from the requirements of international organizations, they contributed to the strategic development priorities of the countries and secured long-term economic growth and human development.

In the context of forming a trade policy targeting long-term economic growth and human development, it is advisable to take into account key conclusions of D. Rodrik’s theory according to which reforming trade policy is particularly beneficial as a method of institutional reform. From this point of view, a significant criterion is the degree to which such trade reform contributes to the improvement of the institutional environment in the country. For example, free trade may contribute to establishing high quality institutions by helping to solve problems such as corruption and rent seeking behaviour.

However, it should be noted that approaches used in other countries do not always fit into the institutional realities of another country. For instance, the institutional development path required for compliance with the World Trade Organization (WTO) norms may be efficient for countries with diversified economies and high per capita incomes, but inappropriate for countries with low public welfare.

In most cases successful institutional reform combines adopted ingredients with local specifics. For example, China’s dual approach to economic reforms proved very successful by introducing modernization of the planned economy through reinforcement of private incentives and development of competition; but at the same time maintaining state leverages that are not characteristic of market economies. In the same manner, South Korea’s orientation towards international markets during the 1960s was not achieved through liberalization of imports, but through subsidies to exports.

The example of Mauritius’s successful reform of trade policies is also noteworthy. Given the small size of the domestic market, the country needed to develop its export potential. At the same time, the country had production facilities servicing the local market and benefiting from the preferences up to the mid-1980s. Thus, while creating conditions in which exports expand, the government had to take into account the interests of enterprises producing import-substituting goods backed up by protectionist measures.

Given this situation, the government resolved to create a free export zone, which ensured further development of foreign trade and an increase in employment, while maintaining the protective measures for companies producing import-substituting items. In turn, increased employment and income levels made greater trade liberalization possible in the mid-1980s to early-1990s⁴.

The above examples confirm that when establishing the efficiency of and selecting a specific mechanism for reforming foreign trade policies, it is not important how such reforms would facilitate the liberalization of foreign trade,

The criterion for trade policy is the degree to which trade reform improves the institutional environment

⁴ “Women, Gender and Work,” 2001, International Labour Office, Geneva.

but whether such reforms would lead to institutional changes that in future would ensure high economic returns and human development. Countries where market institutions are not sufficiently developed, should implement reforms to create domestic capacity, allowing the national economy to utilize the opportunities that open up with foreign trade liberalization, prior to conducting any reforms related to foreign trade.

The increased openness of foreign trade is then, in most cases an outcome of but not the initial factor for achieving economic development. Therefore, the focus while forming strategies and tactics for trade policies should be moved from that on issues related to ensuring liberalization and increasing foreign trade volumes, to that of the need for improving the quality of institutions, implementing a holistic development strategy, providing for long-term growth and achieving high human development rates.

Chapter 2. Uzbekistan: The Soviet Heritage and Its Impact on Public Welfare and Human Development

According to the human development concept, the main objectives of government policy are to provide each human being with choices in all aspects of his/her life, to improve qualitative parameters of life and guarantee basic human freedoms and rights. Such an interpretation of human development allows foregoing the one-sided and exclusive orientation towards quantitative parameters which only characterize the level of personal incomes. The human development concept allows a wider range of factors and indices to be considered, describing the welfare of a human being and the opportunities for releasing human potential.

In 1990, the United Nations Development Programme (UNDP) published its first Report on Human Development, which outlined the concept of human development, determined its key components and calculated the human development index. As a result, the early 1990s were characterized by changes in the global community's view of development priorities towards the new human development concept.

For Uzbekistan, as with other former Soviet Union countries, this period coincided with structural changes in the political, economic and social systems which impacted upon the human development trends in the country. In terms of human development, in 1990-1991, the USSR ranked among the highest 30 countries globally, although the Uzbek Soviet Socialist Republic (SSR) was one of the lowest ranking of the former USSR where living standards were concerned. For instance, by 1990 over 70 percent of Uzbekistan's population had an income below subsistence level, whereas in the Russian and Ukrainian SSRs, this figure was less than 30 percent.

In addition, as Uzbekistan was part of the Soviet Union and was deeply integrated into the economic systems of other former Soviet Republics and socialist countries, the break with these ties caused difficulties that affected the economic and human development in the country. The specifics of the social and economic systems of the Soviet period, as well as consequences of the broken ties between former socialist republics, had in many ways determined the starting position of the independent Uzbekistan for commencing reforms targeting sustainable economic and human development.

As the sectoral structure of Uzbekistan's economy was oriented towards achieving the overall targets of the Soviet Union, one of the main problems inherited from the command and administration system was the established **irrational commodity-based economy**. The main focus of Uzbekistan's agriculture under the Soviet system was the production of cotton (in 1991, cotton accounted for over 40 percent of gross agricultural produce⁵). The industrial structure based on cotton monoculture, with a low share of sectors manufacturing finished products, created unfavorable preconditions in terms of the human development concept.

Structural changes in the political, economic spheres impacted on human development

⁵ "Uzbekistan: Human Development Report 1995," Tashkent, 1995.

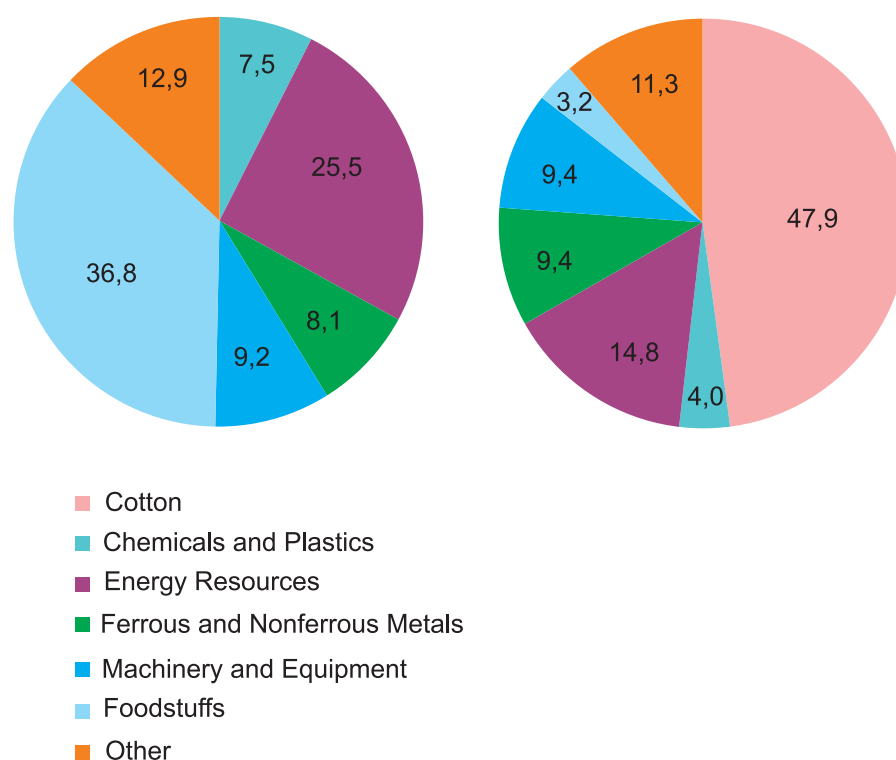
Firstly, as a result of this excessive specialization, during its first years of independence, the country was almost completely depended on imports of staple foods (for example, wheat, potatoes, meat and dairy products), other essential consumer products, as well as strategically important energy resources. In 1992, food imports constituted 36.8 percent of total imports, while energy imports accounted for over a quarter of the country's imports (see Chart 2.1). Given that the lower-income population spends the bulk of its income on food, such a dependence on imports of staple foods created a potential threat for social stability in the society and hindered sustainable human development.

Moreover, the dependence on energy imports, as well as the dominance of cotton in the country's exports, made the country's economy very sensitive to fluctuations in global prices for these commodities.

Secondly, the irrational economic structure with high specialization on cotton was one of the reasons for inefficient employment and hidden unemployment, primarily in rural areas. During the years 1985-1990, while gross national income grew by 16-19 percent, labour productivity decreased by almost 20 percent⁶. Such low-productive employment levels created considerable obstacles for improving public welfare.

The country was almost completely dependent on imports of staple foods

Chart 2.1.
The structure of exports and imports in the Republic of Uzbekistan in 1992



Source: Ministry of Economy of the Republic of Uzbekistan

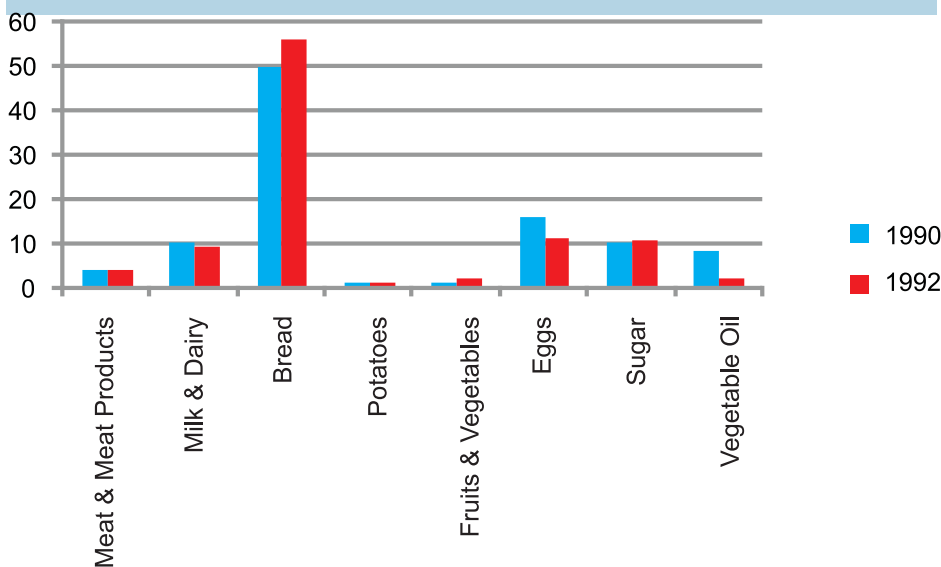
⁶ "Uzbekistan: Human Development Report 1996," Tashkent, 1996.

The complexity of Uzbekistan’s position at the beginning of independence was also due to **the disrupted ecological balance**. The policy of planting monoculture cotton and subsequent expansion of irrigated lands in the Central Asian region implemented during the 1960-1980s, accompanied by inefficient use of water resources became one of the key reasons for river depletion, Aral Sea shallowing and desertification. The unfavorable ecologic situation caused a threat to the health of regional residents and significantly hindered human development in Uzbekistan.

Another major problem was that due to the “money overhang,” accumulated during the 1980s within the system of administrative pricing, the transition from centralized to market economy and liberalization of prices was accompanied by **a spike in inflation and reduction in people’s real incomes**. In particular, retail price growth during 1992 and 1993 was 618.8 and 941 percent, respectively, and in 1992 real disposable income were 70.6 percent of the figure of 1991. In turn, the growth in retail prices and reduction in people’s real incomes had a negative effect on public welfare and became one of the factors responsible for a negative change in people’s diet. In 1992, compared to the respective data for 1990, the share of bread in the diet increased by 6 percent, while the share of eggs decreased from 16 percent to 12 percent, vegetable oil from 7 percent to 3.5 percent, milk and dairy products from 10 percent to 9.5 percent (see Chart 2.2). In the period of 1990-1992, there was also a significant decrease in absolute numbers for annual per capita consumption of certain products: eggs, from 110 pcs to 70 pcs; meat products, from 30 kg to 22 kg; and dairy products, from 210 kg to 170 kg⁷.

The transition to market economy and price liberalization was accompanied by inflation

Chart 2.2.
Energy structure of food products, consumed per day by a citizen of Uzbekistan (as a % of total energy value of all foodstuffs consumed per day)



Source: “Uzbekistan: Human Development Report 1995,” Tashkent, 1995.

⁷ “Uzbekistan: Human Development Report 1995,” Tashkent, 1995.

The government has chosen a strategy of stage-by-stage reformation

It is important to note that administrative regulation of prices under the Soviet system and fixing of prices for energy products (in particular, petrochemicals) at levels much lower than global market prices, had created conditions where **energy resources in production were used in a wasteful manner**. As a result, Uzbekistan, which under the Soviet regime was a net importer of oil, at the time of gaining its independence had an inefficient and uncompetitive industry, the sustainability of which during Soviet times was maintained as a result of artificially low prices for energy products.

However, the system of allocating large budgets for financing such important human development sectors as education, healthcare, and infrastructure development which existed in the Soviet Union, contributed to the development of human capacity and created preconditions for further sustainable development of Uzbekistan at the time of its independence. For example, by the end of 1990, adult literacy index reached 97.7 percent, while life expectancy at birth was 69.3 years.⁸ In addition, because of the financing of infrastructure development projects from the former USSR, at the time of Uzbekistan's independence, the country had a developed transportation system, well-adapted to its geographical location (42,000 kilometers of highways, 90,000 kilometers of local roads, and 3,500 kilometers of railway).

After gaining independence, Uzbekistan launched reforms in its social-economic and political systems in conditions that had a controversial effect on its development during the transition period. This had largely determined the government's decision to choose a strategy of stage-by-stage implementation of reforms targeting long-term economic growth and high human development indices.

⁸ According to the World Bank.

Chapter 3. Trade Policy of Uzbekistan: Goals and Main Objectives at Different Stages of Reforms

3.1. Reformation of trade policy in the first years after independence

The first years after independence brought formidable difficulties to the Republic of Uzbekistan due to both the complexities of the transition from command-administration system to a market economy and democratic society, and the ending of economic ties with former Soviet Republics and other socialist countries.

In these conditions, to minimize negative trends in human development indices and to maintain social stability in the society, it was vital to prevent a plunge in real incomes of the population or decrease in domestic consumption. The most important instrument in achieving these objectives was the trade policy.

In order to saturate the market with required consumer goods, to reduce the inflation rate, maintain real incomes and prevent the public welfare from deteriorating, the priority in foreign trade policy at the first stage of reform was import liberalization and export restrictions. Liberalization of foodstuff imports was important, as, without such, provision of the population with essential foodstuffs and prevention of people's real incomes from plunging would not have been possible in the conditions prevailing during the early 90s. Besides, given that food is the largest expense for the lower-income population⁹, import liberalization at this stage was one of the important factors securing social stability in society.

On the other hand, due to significant discrepancies between domestic and global prices for Uzbekistan's export items, with a view to preventing prices for such items (which included essential commodities) from reaching global levels, a decision was made to restrict exports. Export restriction policy was also determined by the need to fill the market with necessary consumer goods while production was declining and some of the regular supplies from other former USSR countries were terminated.

Instruments for such a foreign policy were relatively low import duties (5-10 percent of customs value), and application of tariff and non-tariff export limitations: in order to achieve the right balance, export duties reached 40 percent, while from 1992 onwards most exports were undertaken based on quotas and licenses.

After the introduction of a national currency, an important instrument for restraining growth in prices for staple goods (for instance, flour and sugar, which during that period were mainly imported) and preventing a major drop in real incomes of the population was strict regulation of the exchange rate of the national currency. Thus, the exchange rate was rigidly controlled through a complex system limiting access of buyers of foreign currency to foreign exchange, both in terms of the composition and number of buyers and of sales of foreign currencies.

⁹ For example, in the mid 90-s the relationship of consumption of foodstuff to the total consumption for the poor strata of the population was equal to 0.82.

To maintain social stability in the society, it was vital to prevent a plunge in real incomes

However, continued dependence on imports of vital foodstuffs, as well as a number of strategically important items (such as energy products), amidst unstable global markets and uncertain prospects in relations with countries supplying such items, had the potential to become a threat to social and political stability, as well as to the sustainable human development in the country. Therefore, even at the first stage of economic reforms, the government decided to begin incentivizing domestic production of such goods, with a view to achieving food and energy independence. In particular, as part of the oil independence programme, the development of new oil fields had begun. In parallel with this, a programme to increase wheat production had started. This led to areas of cotton production, which prior to this was a monoculture, being reduced by about 15 percent, due to an increase in wheat-harvesting lands.

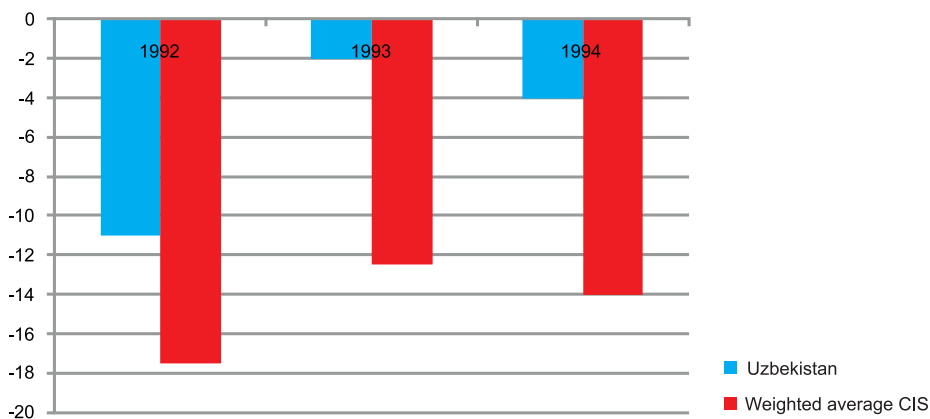
In addition, in order to prevent a rise in poverty and a fall in human development indices in rural areas, during the early years of independence, the government had taken measures to allocate land plots among households, and to increase the sizes of existing private farms. As a result, 650,000 new households received land plots, while 1.6 million households were able to expand their private farms. Thus, the total number of households with land plots reached 2.5 million and the average size of a family plot increased from 0.12 to 0.19 hectares. The implementation of this programme allowed for partial compensation for the significant drop in real wages, by providing rural families with the means of subsistence and acceptable nutrition.

With a view to preventing a major reduction in real incomes, unlike the majority of other countries in transition which had considerably reduced government spending during this period, Uzbekistan maintained government spending at a relatively high level (at least 35.3 percent of GDP during the first stage of the reforms). The state took measures to actively support the real sector of the economy, and to prevent a drop in employment, through state investments, providing subsidies and centralized loans to enterprises.

At the first stage of reforms, the state also exercised an active social policy in order to mitigate against the negative impact of transition reforms on human development. In particular, social transfers had constituted a considerable part (25.2 percent) of total household incomes. In order to prevent a dramatic social differentiation in access to foodstuffs, subsidies were provided for bread, flour, rice, meat, milk, tea, free breakfasts at schools, food coupons for students, subsidies for utilities, and subsidies for pensioners and war veterans.

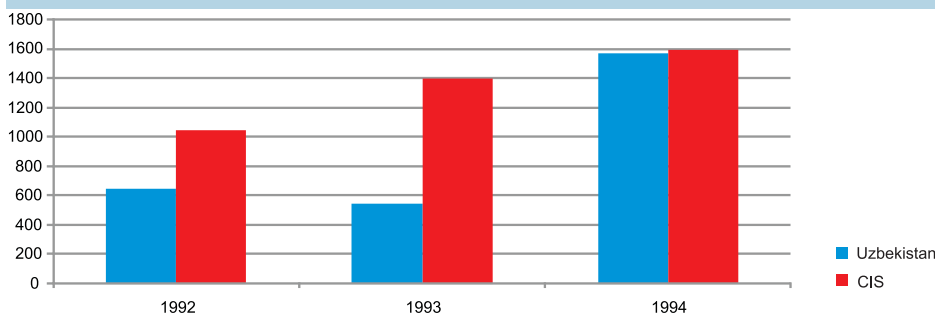
Despite all of the measures taken by the government to prevent a slump in real incomes and human development indices, Uzbekistan was unable to avoid the negative impact of factors related to the collapse of the socialist system and breakup of the Soviet Union. Like other Soviet Republics, Uzbekistan had experienced a considerable reduction in output: during 1992-1994, the GDP dropped by an aggregate of 17.6 percent. However, the decrease in Uzbekistan's GDP during this period was much lower than on average throughout the Commonwealth of Independent States (CIS) – see Chart 3.1) – which is likely to have been determined by the specifics of Uzbekistan's gradual transition to a market economy.

The government decided to conduct a policy aimed at food and energy independence



Inflation in Uzbekistan at the first stage of reform was also relatively favorable compared to other CIS countries (see Chart 3.2), facilitated by the government’s policy of restraining prices in order to prevent a slump in real incomes of the population.

Chart 3.2.
CPI dynamics in Uzbekistan and CIS average, 1992-1994



The government’s policy mitigated the negative impact of the collapse of the command-administrative system

Nevertheless, significant growth in inflation and economic recession caused real incomes to fall: they decreased by about a third in 1992, while in 1994 they were still just over half of the 1991 figure. During this period, poverty surged: according to the First Survey of Household Incomes in 1994, incomes of 44.5 percent of the population were less than the minimum wage, which at that time was close to the poverty level. During 1991-1994, the differentiation of the population by income also increased: the aggregate Gini coefficient increased from 0.26 to 0.31. The decile correlation increased at a slower pace – from 8.5 to 9.3, as thanks to prioritization in budgetary allocations for equalizing transfers to low-income population, the lowest decile’s incomes were protected.

Taking into account the circumstances prevailing during 1991-1994, the government’s policy of the time, mitigating against the negative impact of the collapse of the command-administrative system and complexities of the transition period, must be noted. If all possible consequences of the transition period had manifested themselves to their maximum extent, a more sharp reduction in disposable incomes could have taken place, which in turn could have led to a sizeable decrease in the aggregate demand and considerable drop in human development indices. The gradual nature of

reforms, active social policy, and measures to support the real sector of the economy, allowed Uzbekistan to limit the consequences of the transitional period and maintain social stability in society during the first stage of economic reform.

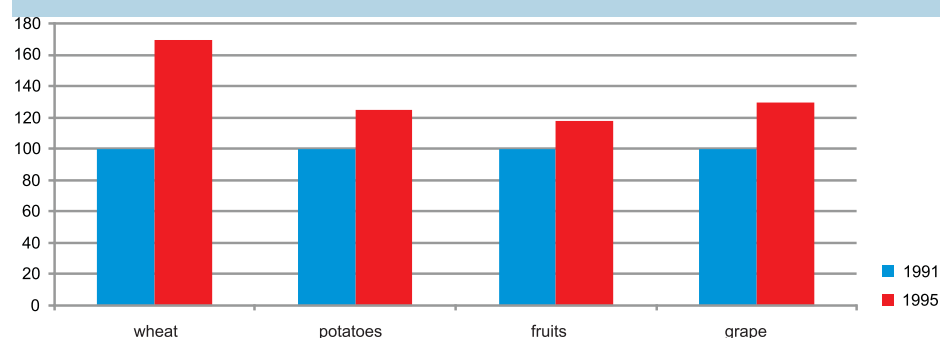
3.2. Trade policy as an instrument of structural transformation

Upon resolving the priority tasks of securing social and political stability, reinforcing the base for the country's independence at the first stage of reforms, the main task of the second stage became the creation of conditions for long-term macroeconomic stability, ensuring positive dynamics in economic growth and human development. To achieve these objectives, the government made a strategic decision in the early 1990s, to achieve grain and energy independence.

The main task was the creation of conditions for long-term macroeconomic stability

When the decision was made in relation to grain independence, the fact that wheat is the main food staple for the country's population was taken into account. The government leveraged administrative controls against large agricultural producers to reorient part of their production from harvesting cotton and other cultures to the production of grains. As a result, by the beginning of the second stage of reforms (in 1995) wheat production had increased by 69 percent - from 0.6 million tons in 1991 to 2.3 million tons in 1995. In addition, within the framework of achieving food independence, production of some other agricultural crops has been increased (see Chart 3.3).

Chart 3.3.
Production of certain agricultural products (as a % of 1991)



The continued dependence on energy imports (in particular, oil) could also have presented a threat to the economic independence of the country and social stability (changes in energy prices have strong effects on other prices), which was behind the decision to pursue import-substitution energy policy.

The implementation of this policy led to an increase in the production of oil and petrochemicals within a short timeframe. As a result, the oil independence programme's goal was reached within just four years of independence – by 1995 (see Table 3.1.).

Table 3.1 Energy balance of Uzbekistan, 1993-1995 (thousand tons)

	1993	1994	1995
Domestic production of crude oil	3944	5517	7586
Oil and Petrochemicals Imports	4762	3153	250
Domestic consumption of oil and petrochemicals	8201	7368	6961
Net imports of oil and petrochemicals	4258	2009	-500

Source: IMF Report, 2000

The programme of achieving grain and oil independence proved very successful: the share of energy imports reduced from 25.5 percent in 1992 to 1.9 percent in 1995, and foodstuff imports dropped from 36.8 percent in 1992 to 18.2 percent in 1995. The fact that such results were achieved has a special importance in terms of securing economic, social and political stability, and achieving high human development results.

The success in implementing import-substitution policies with respect to grains and oil led the government to continue the same policies in other sectors of the economy. To implement such import-substitution strategies, the state maintained a high level of regulation (including administrative methods) in foreign trade and sectoral distribution of resources.

One of the main tools in accelerating reconstruction of the economy and creating conditions for long-term economic and human development, was incentivization of imports of investment goods (primarily equipment for industries listed as priorities by the government) by cutting imports of consumer goods. Since late-1996, the government has also actively exercised exchange policies for these purposes, by introducing currency rationing. Within the new currency regulations, importers of investment goods were given considerable benefits and investments were, in fact, subsidized through the exchange rate. These measures allowed for the trade balance of the country to be controlled and for the redistribution of a significant portion of currency resources for purchasing imported technologies and equipment with a view to modernizing and technical re-equipping of the economy.

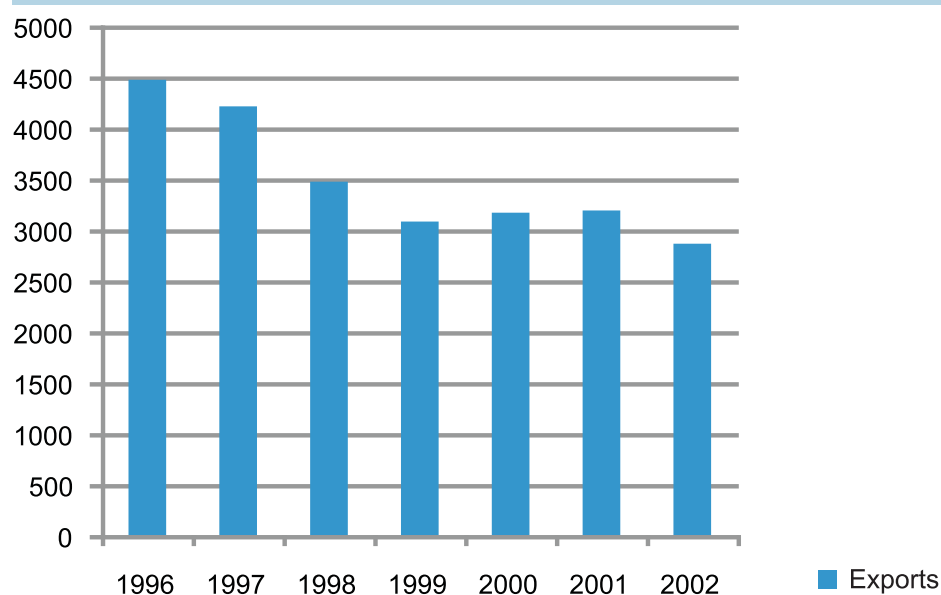
Thus, from 1996, the government has pursued an active industrial policy with the purpose of accelerating the reconstruction of the economy. In addition to access to the official exchange market at an inflated exchange rate for Soum (when importing investment goods), producers of import-substituting goods were given preferential loans and tax preferences.

The import-substitution and currency rationing policy did not always lead to an optimal distribution of currency, borrowings and other resources. For instance, investments into agriculture and construction, the sectors that employ a majority of the country's population, were insufficient. At the same time, some industries have accumulated sizeable idle capacity. In particular, by 2000, utilization of production facilities was high in petrochemical and commodities-based industries, while the same indices for other industries were relatively low. For example, in car manufacturing, utilization of production facilities in 2000 varied by enterprises between 19 percent and 35 percent; in machine engineering, between 10 percent and 20 percent; and in food processing, between 40 percent and 45 percent.

From 1996 the government has pursued an active industrial policy aimed at structural transformation

It must be noted that the introduction of currency rationing and maintaining an inflated exchange rate in Uzbekistan became an important factor that had a negative effect on export volumes. During the years of currency rationing, exports kept decreasing year-on-year, although in part, and such a reduction can be attributed to the deteriorating situation of the country's major export items in global markets (see Chart 3.4). During the period from 1997 to 2002, proceeds from machinery and equipment exports fell from US\$ 277.6 to US\$ 116.5 million; foodstuff exports, from US\$ 163.9 to US\$ 105.7 million; energy and petrochemical exports from US\$ 527.9 to US\$ 243.2 million; and ferrous and nonferrous metals from US\$ 200.4 to US\$ 191.0 million.

Chart 3.4.
Exports from the Republic of Uzbekistan in 1996-2002



Active interference of the state with the distribution of resources led to considerable distortions in such market indicators as exchange rates, interest rates, and relative price structure. Distortion of market indicators in turn led to the distortion in incentives for producers, which had a negative impact on the efficiency of usage of resources and facilitated the development of an informal economy.

One of the results of the second stage of reforms was a considerable redistribution of resources from agriculture into industry. Utilizing the mechanism of a dual exchange rate for cotton producers, the government paid at a considerably inflated official exchange rate, which in fact meant hidden taxation.

Transition towards import-substitution also contributed to the increase in inequality of the population in terms of incomes: in 1995-2000, income inequality grew at a much faster rate compared to during the period from 1991-1994. If in 1994, the Gini coefficient was 0.31, the estimated figure for 2000 (taking into account rent income, interest on capital and entrepreneurial income) ranged between 0,45 and 0,50.

Despite a number of negative effects, the import-substitution strategy made it possible to mobilize resources into basic capital-intensive sectors of the economy (for example, into oil and gas, mining industries), which represent a resource and financial base of industry and ensures its further diversification and modernization. Industrial production growth (from 0.1 percent in 1995 to 5.9 percent in 2000) contributed to the growth of GDP (on average, the economic growth rate during this period was 3.5-4 percent). With the overhaul of production that commenced in 1995-1997, and achieved moderate economic growth, the level of poverty was reduced during the period 1995-2000, by 7.3 percent.

Thus, overall, the results that were achieved in Uzbekistan during this period can be seen as successful, as they helped to create a framework and required conditions for achieving high economic and human development rates in the third stage of reforms. In addition, the shortcomings created a need to amend the economic policy, trade policy inclusive, at the third stage of economic reforms.

3.3. Trade policy in the conditions of developing economic reforms

Given the undesirable consequences of the trade policy pursued during the second stage of reforms, the main objective of the third stage was to achieve high economic and human development growth based on the diversification of the sectoral structure of the economy and activation of market mechanisms.

At this stage of reform, one of the main priorities of economic policy was the diversification of the economy through incentivization of the development of not just basic capital-intensive industries (fuel and energy, ferrous and nonferrous metals), but also those sectors that are labour-intensive (and hence can ensure a considerable growth in employment and public welfare) and at the same time are, or have the potential to become competitive in international markets (for example, chemical, light and food industries).

A key instrument in achieving this objective was the liberalization of the currency market without which export-oriented industries of the economy could not have been developed (these are the most exposed under the policy of inflated exchange rates) or further market reforms could not have been continued. In this context, from 2000, the government began a gradual liberalization of the foreign exchange market and unification of exchange rates with a view to achieving the convertibility of the Soum within current operations. In 2000-2001, a number of measures were taken¹⁰, which resulted in a significant devaluation of the Central Bank-established Soum exchange rate: from 149 Soum per US Dollar in April 2000 to 693 Soum in December 2001. The Soum devaluation rate exceeding the inflation rate caused a decrease in the real rate of the currency and an increase in the competitiveness of domestic producers. Nevertheless, a considerable difference between the exchange rates at the official and parallel markets remained.

The main objective was the diversification of economy and activation of market mechanisms

¹⁰ These measures included: unification of exchange and over-the-counter currency rates beginning on 1 May 2000; transfer of all operations on the domestic currency market (except operations servicing foreign national debt) to over-the-counter exchange rate, from July 1, 2001; unification of Central Bank and over-the-counter exchange rates from November 1, 2001, by devaluing the former to the level of the latter.

Following this, the Government continued implementing measures to devalue the official exchange rate. In particular, between January 2002 and September 2003, the currency was devalued by 40 percent. In addition to this, with a view to unifying official and parallel exchange rates, measures were taken to intensify import protection and tighten monetary and fiscal policies. In particular, tightening of the protectionist regime involved the following measures:

- increased taxation of imports for legal entities by introducing import duties on goods, to be paid alongside the effective customs fees;
- abolishing preferential customs fees for legal entities importing consumer goods;
- expanding the list of goods subject to excise tax while being imported into the territory of the Republic of Uzbekistan, and increasing excise tax rates for certain imported items;
- introduction of flat rate duties – 50 percent for foodstuffs, and 70 percent for non-foodstuffs, as a replacement of 50 percent duty collected from consumer imports by physical individuals¹¹.

Along with these, and with a view to tightening fiscal and monetary policies, from 2002, centralized loans to the real sector of the economy were discontinued and state budget deficits from this period did not exceed one percent of GDP.

As a result of the above measures, the Central Bank and parallel market exchange rates were successfully unified, and from October 15, 2003, the country officially introduced Soum conversion under current international operations, pursuant to Article 8 of the International Monetary Fund (IMF) Agreement.

Trade policy measures, implemented by the Republic of Uzbekistan from 2002, have made a major contribution towards positive dynamics in basic foreign trade indices during 2003-2008 (see Chart 3.5).

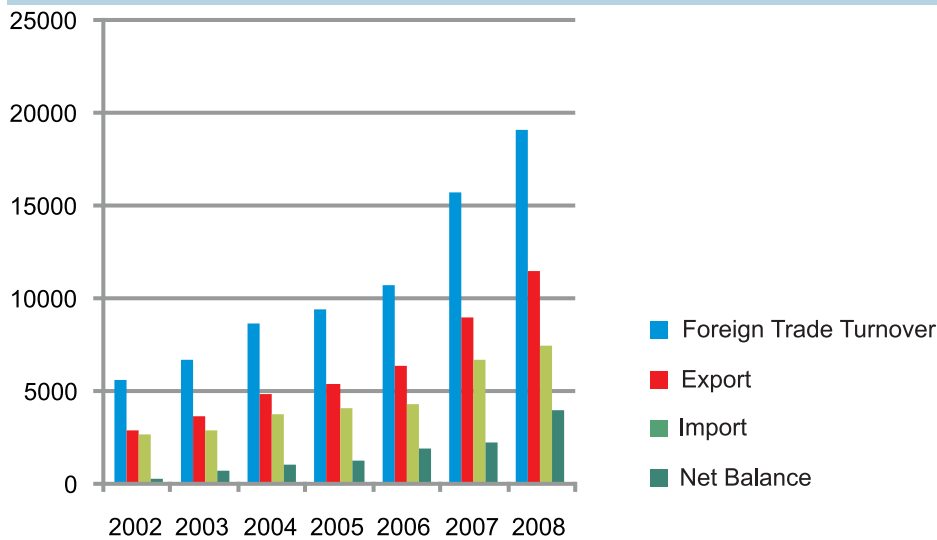
During the period 2003 to 2008, the country saw sustainable growth in its foreign trade: in 2008, the country's foreign trade turnover in monetary terms constituted US\$ 19.1 billion compared with US\$ 6.7 billion in 2003. This included a more than three-fold increase in exports, while imports increased by 2.5 times (see Appendix 2). In 2008, the export surplus increased more than five-fold compared to the same figure for 2003, and represented over US\$ 4 billion.

The high rates of growth in Uzbekistan's foreign trade during 2003-2008 can be attributed to both external and internal factors. The increase in exports resulted from the spike in global prices for the main commodities exported by Uzbekistan (particularly just before the crisis). The liberalization of the currency market, eliminating disproportions caused by distortions of multiple exchange rates, as well as the unification and devaluation of the local currency's exchange rate, also contributed to the considerable increase in the competitiveness of the country's exports.

¹¹ Sirajiddinov, N.S., "Problems of Boosting Uzbekistan Foreign Trade Efficiency," "UWED," Tashkent, 2004.

From 2000 the policy of gradual liberalization of the foreign exchange market has been started

Chart 3.5.
Foreign trade dynamics in Uzbekistan during 2002-2008 (USD million)



Source: State Committee of the Republic of Uzbekistan on Statistics

Along with changes in volumes of exports and imports, the structure of foreign trade also underwent significant changes.

Since independence, considerable changes had taken place in the structural composition of foreign trade (see Appendix 3). The share of cotton fibre in total exports constituted 12.5 percent in 2007, and 9.2 percent in 2008, which is more than a seven-fold decrease in comparison to the early 1990s. The share of other items in total exports was accordingly increasing: ferrous and nonferrous metals from 4.7 percent in 1995, to 11.5 percent in 2007, and 7 percent in 2008; energy products from 11.7 percent in 1995, to 20.2 percent in 2007, and 25.2 percent in 2008; and machinery and equipment from 2 percent in 1995, to 10.4 percent in 2007, and 7.5 percent in 2008 (see Appendix 3). Overall, these changes represent a shift from exports of agricultural commodities towards exports of industrial items.

The implementation of social and economic reforms during the third stage had some positive results: as a result of the liberalization of the currency market and implementation of sectoral development programmes, exports increased. A considerable decrease in the real exchange rate instigated a change in the structure of exports, a gradual decrease in the share of basic commodities and an increase in the share of industries producing non-primary goods. The share of chemical products in exports grew from 2.7 percent in 2002 to 5.6 percent in 2008; machinery and equipment nearly doubled from 3.9 percent in 2002 to 7.5 percent in 2008, while the share of cotton fibre dropped from 22 percent to 9.2 percent. The growth in the share of non-primary goods in total exports contributed to the growth in employment and personal incomes: annual growth rate in real monetary incomes increased from 118.9% in 2003 to 125.1% in 2008. In addition, the poverty level was reduced from 27.5 percent in 2002 to 23.6 percent in 2007. The high economic growth rates were accompanied

Liberalization of the currency market and implementation of sectoral development programmes led to increase in exports

by increased budgetary expenditure in the social sphere¹², which also contributed to improved human development indices (Box 1).

Box 1. Outcomes of reformation of Uzbekistan in transition period

In general, Uzbekistan's heterodox policies have served fairly well. It was able to successfully moderate the hardships of its early transition, resume credible rates of economic growth by the late 1990s, and substantially restructure its economy to be more self-sufficient in such critical items as energy and food.

Its restructuring has enabled it to avoid some of the worst effects of the food and fuel crisis of mid-1998 and the global financial crisis and recession of 1998-1999. By any standard barometers of economic performance—as well as by comparison with other low-income countries—Uzbekistan has been relatively successful over two decades of transition and development, though its achievements appear to remain a frustrating puzzle to many orthodox economists.

"The Puzzling Success of Uzbekistan's Heterodox Development" (one-pager), Terry McKinley, Centre for Development Policy and Research, 2009.

In summary, the trade policy pursued by the Republic of Uzbekistan since independence facilitated social stability at the first stage of reform and creation of appropriate conditions for long-term economic growth and high human development results at subsequent stages. However, the global financial and economic crisis that broke out in 2008-2009, had a significant effect on the achievement of sustainably high economic growth rates and accelerating human development growth rates in Uzbekistan. The following chapter analyses the impact of the 2008-2009 global crisis on Uzbekistan.

¹² In particular, the share of state budget expenses increased from 9.1% in 2004 to 9.6% in 2008.

Chapter 4. The Global Financial and Economic Crisis and Its Impact on Uzbekistan

4.1. The 2008–2009 Global Crisis: Channels of Transmission on Economic Indicators

Due to the low integration of the country's financial system into global financial markets, the global financial and economic crisis that broke out in 2008 had largely an indirect effect on Uzbekistan's economy. The main factors of influence of the global crisis on Uzbekistan were international trade and international remittances.

International Trade

One of the consequences of the global financial and economic crisis for Uzbekistan was a global decrease in demand for various export items of the country in foreign markets and a drop in their global price. For example, in comparison with the first nine months of 2008, proceeds from cotton fibre exports in 2009 decreased by 31,1 percent; ferrous and nonferrous metal exports by 40,7 percent; chemical products by 24,4 percent; and machinery and equipment by 69.7 percent¹³.

The slump in proceeds from machinery and equipment exports in 2009 can be attributed to a sharp decline in demand for cars exported by Uzbekistan into the Russian market (the main export market for Uzbek-made cars). The considerable decrease in export proceeds of cotton fibre and ferrous and nonferrous metals during the same period was due to major changes in global prices for these commodities as a result of the crisis. These changes are likely to have had a negative effect on those employed in these industries.

At the same time, as a result of the global financial and economic crisis, the demand for and global price of gold has increased, which had a positive effect on the country's trade balance. A rise in the price of exported gas, resulting from the transition to the European formula for determining gas prices, beginning on 1 January 2009, also contributed to the increase in export proceeds (a rise of 76 percent for the first nine months of 2009, compared with the respective period for the previous year).

As a result of the trends in changes in global prices for the country's export items, as well as the timely development and implementation of the 'Anti-Crisis Programme', aiming to support exporters and stimulate domestic demand (see Section 5.1) during January-September 2009, the volume of exports fell by only 5.4 percent. In financial terms, the export surplus exceeded US\$ 2.3 billion and GDP grew by 8 percent.

Changes were also observed in the structure of the country's imports. In

The global financial and economic crisis led to a global decrease in demand for exports

¹³ "Economy of Uzbekistan," Informational and Analytical Review for January-September, 2009, CER, 2009.

particular, during the first nine months of 2009, the share of energy and oil products decreased from 5.3 percent to 3.1 percent; and ferrous and nonferrous metals from 7.9 percent to 6.2 percent. These changes were largely caused by the drop in global prices for these items. At the same time, the shares of foodstuff imports and machinery and equipment imports increased (from 8.1 percent to 8.9 percent and from 50.3 percent to 57.5 percent, respectively).

Fluctuations in prices and export volumes, as one of the consequences of the global financial and economic crisis, determine the need for and emphasize the importance of state policy measures aiming to diversify the structure of, and stimulate non-commodity based exports.

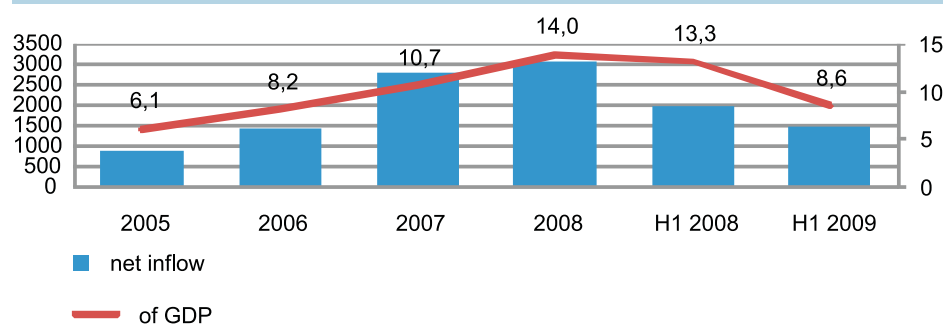
International Remittances

Remittances into Uzbekistan fell by over 30% during the first half of 2009

International remittances were another channel of influence of the global financial and economic crisis on Uzbekistan. During recent years, remittances from labour migrants represented a significant share in Uzbekistan's GDP and became one of the main sources of income for a considerable part of the republic's population (see Chart 4.1). Moreover, during 2006-2008, remittances underwent a dramatic increase, from US\$ 1.4 billion to US\$ 3.3 billion.¹⁴ This can be attributed in part to a considerable increase in business activity, observed during the same period in Russia, a country hosting a sizeable number of labour migrants from Uzbekistan.

However, a plunge in business activity in Russia caused by the global financial crisis, especially in real estate and residential construction, which employs most of the labour migrants from Uzbekistan, led to a sizeable drop in international remittances into the country. According to estimates, remittances into Uzbekistan fell by over 30 percent during the first half of 2009¹⁵.

Chart 4.1.
Remittance Dynamics



Source: Calculations based on data from Central Bank of Russia, IMF, and "Impact of Remittances on Uzbekistan's Economy," Analytical Note, CER, 2007

¹⁴ "Remittances Data," Taniguchi and Gulamov; Hashimova; Khakimov and Mahmadbekov, World Bank, 2009.

¹⁵ "Global Financial Crisis: Challenges for Employment, Modernization and Sustainable Growth in Uzbekistan," Analytical Note, CER, 2009.

An increase in the number of labour migrants from Uzbekistan over the past years is in part a result of structural reforms conducted in the agrarian sector, including the establishment and consolidation of farms (see Section 5.3).¹⁶ In turn, growth in the supply of labour in rural areas will continue to create new migration flows, both domestic and external, which would intensify the dependence of households on remittances.

In order to mitigate the consequences of the global financial and economic crisis and to prevent a sharp decline in economic growth, employment and social stability, at the end of 2008, the government mapped out a large-scale 'Anti-Crisis Programme' of measures.

4.2. Impact of the Financial Crisis on Human Development

The global financial and economic crisis is likely to have had a negative impact on human development prospects in the country.

Firstly, the decrease in demand for the products of exporting companies in a number of industries, especially in labour-intensive sectors of the economy, caused by the crisis, and the subsequent drop in export proceeds, is likely to reduce employment and incomes for those employed in these industries, and lead to a deterioration in the welfare of their family members.

Secondly, a major fall in remittances from labour migrants is likely to lead to a reduction in incomes and a deterioration in public welfare, and as a result, have an unfavorable effect on human development prospects in the country. According to estimates, as a result of the global crisis, in 2009, remittances were reduced by almost US\$ 1 billion, meaning a decrease in disposable incomes of households by 1.5 trillion Soum. This reduction was caused by the decrease in migrant wages, and by the increasing number of returning labour migrants, which also aggravated the labour market situation in the country.

An important factor in mitigating the negative consequences of the global financial and economic crisis on employment, incomes and, consequently, human development, was the timely elaboration and implementation of the Anti-Crisis Programme. The programme envisages a series of interrelated and consecutive economic policy measures, aiming to support exporters, stimulate domestic demand and enhance competitiveness of domestic producers, both in foreign and domestic markets.

An analysis of the government's Anti-Crisis Programme shows that the developed and implemented measures can be nominally divided into two groups:

1. Measures directed towards overcoming negative consequences of the global financial and economic crisis.
2. Measures directed towards boosting the competitiveness of the domestic economy in the mid- and long-term run.

It is important to emphasize that the division is nominal. This is due to the fact although the first group of measures were developed and are being implemented based on the potential areas of impact of the global financial and economic crisis on the social and economic situation in the country, they

¹⁶ Consolidation of farms means merging two to three small and medium-sized private farms to create one private farm with a large land plot.

An important factor in mitigating the negative consequences of the global financial crisis is the Anti-crisis Programme

have, without any doubt, an important role in the country's social and economic development post crisis. Along the same lines, the implementation of measures aiming to boost the domestic economy's competitiveness in the medium- and long-term is an important factor in coping with negative consequences of the global financial and economic crisis in the short-term.

Important measure in overcoming the negative consequences of the global financial and economic crisis and to boost the competitiveness of local producers, are support for and maintenance of stable operations of exporting enterprises, creation of additional incentives for exports in response to deteriorating trends in international markets, and preventing exporter incomes from plunging, and consequently having serious negative consequences for human development indices in the country. These measures include both credit and budgetary support to exporters:

**Anti-crisis measures are aimed at:
– overcoming negative consequences of the global financial and economic crisis
– boosting the competitiveness of the economy**

- Allocation of preferential loans by commercial banks, for working capital needs for periods of up to 12 months, at rates not exceeding 70 percent of the Central Bank's refinancing rate;
- Extending all tax and duty exemptions, except for value-added tax, for entities with foreign investments specializing in the production of finished products, until 2012;
- Restructuring overdue and current debts under bank loans and writing off budgetary penalties, as well as providing other benefits and preferences
- Increasing capitalization of major banks with funds from the budget, the Reconstruction and Development Fund, and other shareholders;
- Enhancing the competitiveness of companies by tightening expenses, and stimulating the reduction in manufacturing expenses and the cost of products. The Anti-Crisis Programme envisaged the development of an effective mechanism to incentivize the management and executive staff to achieve planned figures in terms of cutting costs;
- Increasing the flexibility and independence of companies in terms of pricing for exported items.

Another set of measures of the Anti-Crisis Programme aim to stimulate domestic demand for the products and services of local producers, which not only compensates for the lower demand from foreign consumers, but also helps to create new jobs and increase personal incomes. These include the following measures stipulated in the programme:

- Expanding the production of localized goods 3-4 times;
- Incentivizing production of food and non-food items through a wide range of additional fiscal incentives to domestic producers until 1 January 2012;
- Providing pricing preferences of up to 20 percent to local producers participating in bids under state procurement of goods and services;
- Further development of production and social infrastructures, as important factors of modernization of the country and increased employment;
- Expanding the scope of residential construction, reconstruction and repair;
- Incentivizing the development of small businesses and the service industry.

Economic crises are characteristic of the global economy and have a cyclical nature. As the global economy is recovering from the crisis, the strategic benefit remains with those countries that were able to maintain, reconstruct and increase their production capacity. Therefore, one of the main benefits of Uzbekistan's Anti-Crisis Programme is its special emphasis on the acceleration of structural reforms in the economy and creation of the base for sustainable growth and human development in the long run, focusing on those strategic priorities and projects related to production modernization, technological re-equipment and diversification, which are already being implemented in Uzbekistan¹⁷.

It is also important to note that the measures to expand production and social infrastructures, were adopted with a view to support investment activity, and targeting the acceleration of social transformation and changes in the population's lifestyle.

The Anti-Crisis Programme provides for the expansion in the construction of educational institutions (colleges, academic lyceums, schools and sports facilities). During the period January-September 2009, 350 billion Soum of investments was utilized in new construction and capital refurbishment of comprehensive schools, constituting 14.3 percent of non-production investments and 37.4 percent of investments in education. Along with this, investments into the construction and refurbishment of academic lyceums and professional colleges constituted 513.5 billion Soum (20.9 percent of total non-production investments and 54.9 percent of investments into education).

In addition, during January-September 2009, 77.7 billion Soum of investments were made in the construction of water distribution networks, and 6.5 billion Soum of investments in the construction of gas networks; construction of the Uzbek national highway was extended by 1,501 km; and the implementation of railway electrification projects was accelerated.

The establishment of a free industrial-economic zone at Navoi city airport and the transfer of the management of the newly built airfield in Navoi to an international operator (Korea's Korean Air) was an aspect of the successful Anti-Crisis Programme of Uzbekistan, aiming to boost the competitiveness of the domestic economy and improve human development indices. Businesses operating within the Navoi free industrial and economic zone are mostly involved in the production of a wide range of highly technological and internationally competitive products, through the introduction of contemporary high-performance equipment and machinery, technological lines and modules, and innovative technologies. In addition, the creation of an international intermodal logistics center will allow for it to be used as a transcontinental transportation and forwarding hub, connecting South East Asia with Europe. The transcontinental multimodal logistics centre in this zone is the first in the CIS territory, and it reduces the distance for international air shipments from South and South East Asia to Europe and Northern America via the Navoi hub by three times. The hub is expected to efficiently process shipments, distribute and store them, and is expected to become an important link in global cargo transportations.

The implementation of *The Year of Development and Improvement of Countryside*, a state programme approved in 2009, is a component of the Anti-Crisis Programme.

¹⁷ Namely, the Government's Anti-Crisis Programme proposes the implementation of about 300 investment projects for a total amount exceeding USD 24.0 billion.

Anti-crisis programme was focused on the acceleration of structural reforms in the economy

The adopted anti-crisis measures prevented a significant deterioration in human development

This stipulates a wide range of long-term interconnected measures aiming to fundamentally improve living standards in rural areas; accelerate development of social and production infrastructure; completely reconsider the status, role and importance of the owner, entrepreneurship and small business; provide comprehensive support to farm development; and establish new and modern processing companies equipped with compact technologies, in rural areas. As part of the Programme of the Year of Development and Improvement of Countryside, a special bank for rural construction and repair was established and construction companies were set up in each district.

Within the Anti-Crisis Programme, measures to optimize the structure of agricultural crops were also adopted. Among these, the key ones involve reduction of areas for cotton and their usage for oil crops and vegetables. The adopted measures enabled the achievement of high growth rates in yields of potatoes (56.5 percent), vegetables (20.4 percent), and fruits and berries (18 percent) in 2009, compared to the respective figures for 2008.

These measures, along with the implementation of a series of measures to improve the ameliorative state of the lands, as provided by the 2008-2012 State Programme for Ameliorative Improvement of Irrigated Lands, will become an important factor in the growth of the competitiveness of local agricultural producers and living standards of the rural population. The programme provides for the maintenance of current irrigation and melioration sites in proper technical condition, improvement of the facilities of special water management, construction and maintenance organizations, and equipping them with modern machinery. Bearing in mind that over 60 percent of the population live in rural areas, improving the rural population's welfare and living standards are an important factor in Uzbekistan.

In order to mitigate the consequences of reduced migration from the country, a targeted employment programme was adopted as part of anti-crisis measures, whose implementation created 743,500 new jobs during January-September 2009.

The adopted anti-crisis measures enabled some of the negative consequences of the financial crisis to be mitigated and prevented a reduction in economic growth rates, employment, social stability, and, consequently, prevent a significant deterioration in human development in the country. For example, in the first nine months of 2009, the programme did not only succeed in preventing a slump in real personal incomes, but actually enabled them to grow by 30 percent compared to the same period of 2008.

The measures introduced by the Anti-Crisis Programme assisted in overcoming some of the negative consequences of the global financial and economic crisis on employment and personal incomes. They can also provide a boost to the competitiveness of the domestic economy in the post-crisis period of the country's social and economic development, which will be an important additional factor for human development in the medium- and long-term.

However, despite the adopted measures, there is still a considerable potential and further opportunities for the acceleration of economic growth and human development, and not least through a stronger role of the trade policy in this process. To realize this potential involves further implementation of economic reforms.

Chapter 5. Main Directions in the Improvement of Trade Policy with a View to Achieving High Human Development Results in the Post Crisis context

Trade policy and development of foreign trade are important factors in the economic and human development of the country.

Firstly, increased exports (and especially, growth in exports of non-commodity based products with high value addition and the role of exports in labour-intensive industries) can contribute to the **growth in productive employment, and increase in the incomes of those employed in export-oriented or related industries and their family members**. These additional incomes can be used for: the improvement of qualifications or education of family members, and thus contribute to the general level of education; and purchasing of medicines and payment for medical services, improvement of diets, providing more opportunities for a healthy lifestyle, and thus contributing to better health and longer life expectancy. Growth in production and export volumes in industries, which, percentage-wise, employ more women (for example, the textile and apparel industries), can considerably increase the employment, incomes and living standards of women, and contribute to gender equality.

Secondly, additional proceeds from foreign trade can be redistributed **through the state budget** and used to support the low-income and most vulnerable layers of the population, to develop secondary and higher education systems, public healthcare, social infrastructure, and implementation of various social programmes aiming to provide for gender equality. In particular, in a globalized world, quality education can benefit from access to foreign training materials, equipment, educational technologies; while an efficient healthcare system and improvement of public health can take advantage of access to foreign drugs, medical services and equipment.

Thirdly, a change in the structure of foreign trade towards more complex, 'highly-productive' items sets **higher requirements for labour force qualifications**, which stimulates the development of the educational system.

Fourthly, exports and imports expand **the choices** both for domestic consumers (imports), and for domestic producers (exports), which is an important condition of human development.

The experiences of a number of foreign countries indicate that in order to facilitate sustainable economic and human development, a trade policy should be based on the overall development strategy of the specific country, and be an integral part of the national development strategy, along with reforms in other spheres (see Chapter 1).

Trade policy is an important instrument in enhancing a country's potential for sustainable development. It is advisable to begin reforms in trade policy by building domestic capacity (private sector, public sector, human resources), which in future will enable utilization of the opportunities that emerge during reforms in the area of foreign trade.

Trade policy is the important factor of the economic and human development

Based on the above, in order to maximize the potential of trade policy for the purposes of human development, reforms in the following areas are recommended:

- Building domestic capacity of the private sector and the state with the purpose of improving competitiveness;
- Improving the quality of the workforce and human development;
- Developing a trade policy strategy aiming to achieve high economic and human development results in the long run;
- Implementing reforms targeting increases in employment and personal incomes (for example by incentivizing production and exports in labour-intensive sectors), and developing the agricultural sector;
- Developing transportation and transit as important factors of an efficient trade policy targeting sustainable development.

The aforementioned reforms targeting human development will be reviewed in detail in Sections 5.1–5.5.

5.1. Improving the Competitiveness of the Economy

It is advisable to begin reforms in trade policy by building domestic capacity

Whether a country would benefit from its expanded participation in international labour markets and international trade is largely dependent on the level of the competitiveness of its economy. In a country, where most of the producers are not competitive in the global market, a sudden liberalization of the trade policy may lead to significant structural consequences, which could have a negative effect on human development indices. On the contrary, in a country with competitive producers, appropriate institutions and a high level of human resource development, transition to a liberal trade policy may become one of the ways to fully utilize the benefits that the country has, and to achieve sustainable long-term growth and human development. Hence, the level of competitiveness of domestic producers, both in domestic and international markets, largely determines the character of a country's trade policy.

Despite the measures to rebuild the economy on a structural level, taken by the Government of Uzbekistan during recent years, the share of finished products in exports remains low: presently it does not exceed 30 percent, which indicates the low competitiveness of the economy. Growth in the competitiveness of the economy and increased share of finished products in the structure of exports could contribute to growth in highly-productive employment and personal incomes; reduce the country's dependence on the unstable commodity market trends; and subsequently achieve sustainable economic and human development. This emphasizes the importance of developing and implementing state policy measures aiming to increase the competitiveness of the country's economy. The factors, determining the competitiveness of the national economy, include:

- The level of development of the production capacity of enterprises;
- The compliance of manufactured products with international quality requirements and standards;
- Transactional costs of doing business;
- The efficiency of foreign exchange policy.

Each of these factors will be discussed in more detail in Sections 5.1.1.–5.1.4.

5.1.1. Developing the Production Capacity of Enterprises

The development of the production capacity of enterprises is essential for reducing production costs, improving the quality of products, and, therefore, improving the competitiveness of enterprises. Improving the competitiveness and increasing exports through enhanced production capacity of domestic enterprises could facilitate the growth in productive employment and personal incomes.

With a view to developing production potential, Uzbekistan has taken measures to restructure and provide financial support to industrial enterprises, increase the production capacity utilization, and to incentivize the production of finished goods. Among measures taken, the benefits and preferences provided in a number of industries within the following programmes should be noted:

– Localization of the production of finished goods, accessories and materials based on local raw materials. As part of this programme, preferences were given to textile producers, chemical producers, machine engineering, and the electro-technical industry. Total localized production in 2007 exceeded 2.4 trillion Soum – one-and-a-half times more than the previous year, while the share of localized produce in gross industrial output constituted 13.1 percent.

– Development of particular industries. Currently adopted and implemented programmes include: car manufacturers development (2008-2009), pharmaceutical (until 2011), chemical (2007-2011), oil and fat (2007-2011), construction materials (2007-2011), ginning (2007-2011), textiles (2006-2008) and silk (2006-2010) and industry development programmes, together with a railroad industry development programme (2009-2015). In addition to these, programmes for developing Uzmetkombinat JSPA enterprises (2007-2011), and Navoi and Almalyk Mining-Metallurgical Combines (until 2011) are being implemented.

– Annual investment programmes. Pursuant to the Investment Programme for 2010, capital investments will constitute over 30 percent of GDP, having increased by 22.1 percent compared with the previous year. Implementation of production-related investment projects accounts for over 75 percent of all capital investments. In 2010, the implementation of strategically important projects will have attracted over US\$ 3 billion in foreign investments, an increase of more than 30 percent compared with the previous year, while foreign direct investments will have increased by 46 percent¹⁸. The establishment of the Reconstruction and Development Fund of Uzbekistan in 2007 was of great significance in terms of attracting domestic resources in the implementation of long-term strategic investment projects, primarily for building infrastructure, and reconstructing and upgrading production. The Fund is formed with financial resources received from favourable global prices for commodities. To-date, the Fund has accumulated over US\$ 3.7 billion. The Fund's share in total capital investments into the domestic economy during 2010 is estimated at 7.5 percent.

The development of the production capacity of enterprises is essential for reducing production costs

¹⁸ Speech by the President of the Republic of Uzbekistan at the Cabinet of Ministers session on the country's social and economic development results for 2009 and most important priorities of the economic programme for 2010.

The implementation of the above-mentioned measures facilitated the achievement of high growth rates in machine engineering and metal works, ferrous metal industry, production of construction materials, knitwear, apparel, and foodstuffs. The annual growth rate of industrial production in 2007 was 12.1 percent compared to 5.7 percent in 2002.

Nevertheless, the low share of finished products in total exports of the country, and an insufficiently high level of capacity utilization in certain industries indicates the need to take further measures to boost the production potential of the enterprises.

One of the important instruments in the development of the production capacity of enterprises in Uzbekistan is *the implementation of strategic directions and projects to modernize, reequip, and diversify production*, including projects stipulated within the Anti-Crisis Programme. These measures provide for the completion of the earlier sector modernization programmes, adopted for 2009-2012, and the implementation of new strategic investment projects in basic sectors of the economy during 2009-2014. It is expected to complete approximately 327 investment projects for a total amount of over US\$ 42.5 billion. The modernization projects cover fuel and energy, chemical industry, oil and gas processing, metallurgy, light and textile industries, construction materials, machine engineering and other sectors of the economy. Among these, new construction projects are expected to use up approximately US\$ 31.3 billion; modernization, reconstruction, technical and technological re-equipment projects are expected to cost US\$ 9.8 billion; and US\$ 1.4 billion would be used for other purposes.

These measures are interconnected with the continuing reforms in banking, incentives for raising the population's and entities' uncommitted funds as deposits to commercial banks, and increasing capitalization levels of the banks. According to estimates, the implementation of these projects would create an additional annual production worth US\$ 10.4 billion, a US\$ 6.5 billion increase in annual exports, and a significant growth in GDP, through the introduction of innovative and energy-saving technologies, and mastering the production of new kinds of goods that are in demand in international markets. Furthermore, the introduction of innovative technologies and incentivization of the interaction between production and research sectors would help to maintain and develop the scientific potential of the country.

In addition, the production capacity of the economy can be expanded and, subsequently, the competitiveness of enterprises can increase with the introduction of new institutions to implement the industrial policy, such as national and international business groups. The establishment of business groups that are capable of integrating into international value chains, would ensure accumulation and utilization of resources for the development, modernization and technological improvement of production, incentivization of innovative development and, consequently, increase the competitiveness of the economy. The integration into global value-addition chains can facilitate the inflow of capital into the country, in the form of investments and technologies, the introduction of new management techniques, the creation of productive jobs, and, as a result, the human development of the country (see Box2).

An important instrument of development of the production capacity is the Programme of modernization of the economy

Box 2. Measures to create the favourable conditions for business-groups

In order to create favourable conditions for business groups it is important to make amendments to existing legislation and implement measures aimed at stimulating cooperation of enterprises. In particular, recommendations include:

- Stimulating the integration of enterprises of the real sector (including enterprises involved in export industries) and preventing a decrease in the number of large enterprises in the manufacturing, transport and construction sectors;
- Completing the process of transferring government functions to government ministries and agencies and differentiating the responsibilities of the executive power and the production sector;
- For exporting business-groups, abolishing excessive taxation and implementing the single taxation (of value-added);
- Introducing for business-groups the procedure of consolidated financial reporting, taxation and audit, that will solve the problem of non-payments, and optimize payments within business-groups.

Business-groups in Uzbekistan: mechanisms of formation and stimulation, policy paper, CER, 2009.

5.1.2. Improving the Quality of Products

Amidst intense competition in external markets, one of the main factors boosting competitiveness is the improvement in the quality of manufactured products by introducing international standards and requirements.

The ISO standard system is an international standard allowing for the control of the quality of products at all stages of the manufacturing process.

Pursuant to ISO, entities must comply with the requirements on a number of elements, including:

- 1) *general quality management of products*¹⁹;
- 2) *management of an entity's technological processes*²⁰;
- 3) *personnel qualification criteria*²¹;
- 4) *quality standards to ensure quality at final checkups and testing*²².

ISO participants today include over 150 countries globally, with each represented by its national standardization agency. The Republic of Uzbekistan, represented by its Uzstandard Agency, is a fully-fledged member of ISO with voting rights, since 2000.

In order to stimulate the introduction of a quality control system in accordance with international standards, the Government has adopted

¹⁹ Standards for enterprise organizational structure and authority distribution.

²⁰ Standards provide for the traceability of any item during the production: introduction of marking and other ways for identifying, compliance of the equipment, used at an enterprise, to established standards.

²¹ According to this standard, all employees are evaluated in terms of their skills providing for the quality of their work: job descriptions, qualification requirements, training needs.

²² Internal quality inspections, warranty and post-warranty service.

The main factor boosting competitiveness is the improvement in the quality of products

respective regulatory acts at various Uzbekistan enterprises²³. As a result, the State Registry of Certified Quality Management Systems lists approximately 200 entities.

The introduction of the ISO international standard system can facilitate a considerable reinforcement of the competitiveness of enterprises. Namely, the fact that the production has a certified quality management system can become one of the main factors in selecting such an enterprise as a business partner: the introduction of standards, as a rule, ensures a high level of trust to such enterprises from consumers, and therefore boosts the demand for such an entity's produce. The standards are also an effective mechanism of communication with all levels of production personnel, which allows for timely responses to changes in market demands.

For this reason, further stimulation of the introduction of international quality standards at various enterprises could become an important factor boosting the competitiveness of the economy of the Republic of Uzbekistan. The modernization of the industry and quality control from the very beginning of the manufacturing process will allow goods to be produced that comply with international requirements, thereby contributing to the increase in exports of finished products. In addition, the orientation towards the production of goods complying with global quality standards, would allow for optimizing the usage of funds allocated under the Modernization Programme, which is one of the determinant development programmes during the post-crisis period. Another important aspect is that the introduction of international standards at all stages of the manufacturing process can increase the skill levels of the workforce, and, as a result, facilitate human resource development.

The competitiveness of domestic producers is determined by transaction costs of doing business

5.1.3. Transactional Costs of Conducting Business

The competitiveness of domestic producers is largely determined by the transactional costs of doing business, which, in turn, depend on the business climate in the country. Improving the business climate could also lead to the mobilization of family assets into business.

Given the considerable importance of the reduction of transactional costs of doing business to achieve sustainable growth and reduce the level of poverty amongst the population, since independence, Uzbekistan has been implementing a series of consistent measures aiming to reduce the transactional costs of doing business and create a favourable business climate in the country.

²³ Resolution No. 173 of the Cabinet of Ministers of the Republic of Uzbekistan dated 19.06.2009, On Additional Measures to Expand the Introduction of Quality Management Systems at the Republic's Enterprises, Conforming to International Standards; Resolution No. 183 of the Cabinet of Ministers of the Republic of Uzbekistan dated 29.08.2006, with amendments No. 96 dated 11.05.2007, On Additional Measures to Introduce Quality Management Systems at Enterprises, Conforming to International Standards; Resolution of the President of the Republic of Uzbekistan No. PP-1050 dated 28.01.2009, On Additional Measures to Stimulate the Expansion of Production of Domestic Nonfood Consumer Goods; Decree of the President of the Republic of Uzbekistan No. UP-4058 dated 28.11.2008, On the Programme of Measures to Support Enterprises of the Real Sector of the Economy, to Ensure their Stable Operations and to Increase Export Potential; Decree of the President of the Republic of Uzbekistan No. UP-3937 dated 12.11.2007, On Measures for Further Reinforcement of Inter- and Intra-Sector Industrial Cooperation.

Box 3. Perspectives of development of the private sector

According to the results of surveys, households of Uzbekistan have assets of US\$ 85-87 billion compared with US\$ 35 billion in 2003. During this period the share of households, taking steps to use their assets for launching the business increased twice, while the percentage of successful attempts increased from 60 to 90. It is important to implement measures aimed at involving more households and the economically active population in business by providing financial and other support on the first stages.

The perspectives of formation of new sources of economic growth, as well as the qualitative changes, will mostly depend on whether the private sector is willing to be a partner of the government, adopting the long-term priorities and aims of government programmes.

Now is a crucial time for the enterprises class in Uzbekistan. The period of accumulating capital is over. The transition to new, more complicated types of business activities has started. These activities require new knowledge and skills, more advanced technologies and more investment. Therefore, the main focus should be on creating conditions to stimulate large enterprises, technological modernization and diversification of production.

Material of the research Family assets mobilization - 2010.

The policy to further reducing the tax burden is recommended to be continued

One of the main factors determining the transactional costs of doing business and the competitiveness of domestic producers is the tax **burden**. Taking this into account, the government has been implementing a series of measures to steadily reduce the tax burden and simplify tax administration. These measures include:

- cancellation of the ecology tax²⁴, which constituted 1 percent of costs;
- a considerable simplification of tax payments for small businesses. For instance, for micro-firms and small businesses, the aggregate tax burden including unitax, compulsory allocations to non-budget Pension Fund and School Education Fund, were replaced with a unified tax payment, and as a result, reduced from 15.2 percent in 2004 to 10 percent in 2007;
- gradual decreases in unitax, unified social fee, personal income tax and corporate income (profit) tax. For example, during 2004-2007, the corporate income tax rate was reduced from 18 percent to 10 percent, unified social fee rate – from 31 percent to 24 percent, maximum personal income tax – from 30 percent to 22 percent;
- expansion of the list of business expenses deductible from the taxable base for the purposes of the corporate income tax;
- adoption of measures to streamline tax inspections, to simplify tax reporting procedures (here, the introduction of desk audits can be noted in particular) and to reinforce mechanisms for protecting the rights of taxpayers.

In 2007, the new edition of the Tax Code was adopted. It systematized, unified

²⁴ The tax rate was not based on the real damage that a specific entity was inflicting upon the environment; hence the tax did not provide incentives for the reduction of hazardous emissions and other pollution.

and simplified the tax legislation, especially in terms of tax administration, and describes in detail various procedures for the interaction of state bodies and entrepreneurs in the area of taxation. The new edition includes the principle of the direct application of the Tax Code and premises for stabilizing the tax system. Tax preferences, especially the inefficient and unutilized ones, were reduced and systematized. Sections were included to regulate forms and procedures for tax inspections, as well as for appealing against decisions of tax bodies and actions of their officials, which is extremely important from the point of view of protecting the rights of taxpayers.

With a view to overcoming the consequences of the global financial and economic crisis, a number of additional tax benefits and preferences were granted to entities as part of the Anti-Crisis Programme (see Box 4).

Box 4. Measures of Financial and Credit Support to Entities as Part of the Anti-Crisis Programme of the Government of the Republic of Uzbekistan

With a view to overcoming the negative consequences of the global financial and economic crisis, ensuring sustainable economic growth and macroeconomic balance, contributing to the employment and providing targeted support to exporters and small businesses, resolutions of the President and Cabinet of Ministers of the Republic of Uzbekistan provide a number of benefits and preferences, including:

- providing benefits to the producers of consumer goods and reducing unitax rate for small businesses involved in industrial production, from 8 percent to 7 percent;
- restructuring of overdue and current debts under bank loans, writing off fines and penalties of certain export entities, which are implementing new construction, modernization, technical and technological re-equipment of their production and are experiencing temporary financial difficulties due to reduced export prices and demand for export items;
- increasing the term of commercial bank guarantees, issued to textile companies for procuring cotton fibre from foreign trade companies, from 90 to 120 days;
- simplifying procedures and reducing the timeframe for returning VAT to 20 days, for exporting companies, and using offset mechanism accounting for current and future budgetary liabilities;
- temporary (only during 2009) extension of the period after which tax bodies accrue penalties for untimely receipt of export currency proceeds for shipped products, provided that the amount is received in full, from 30 to 60 days;
- extension of tax benefits, given to foreign investment entities specializing in the production of ready-made clothing, until 2012 (Decree of the President of the Republic of Uzbekistan No.UP-3267, dated 20.07.2003);
- extension of exemption from customs duties for imported raw materials and supplies for textile products, until 2012 (Resolution of the CM No.141, dated 25.03.2004).

Source: *Cost of Doing Business in Uzbekistan, 2009, UNDP*

The policy for further reducing the tax burden is recommended to be continued. In late-2008, State Budget income represented 23.7 percent of GDP, which is significantly higher than in other developing and transitional economies. For example, in China, during the years of its phenomenal economic growth (1979-1996), the total tax burden was reduced from 36 percent to 13 percent, and only afterwards (after 18 years of record economic development) was it increased to 20 percent.

The most criticized tax among entrepreneurs are **high labour taxes**

(personal income tax and unified social fee), which limit the opportunities for increasing employment and force entrepreneurs to look for 'grey' schemes of doing business; and gross revenue taxes, which deduct a sizeable portion of net incomes of companies. The tax regime in Uzbekistan currently carries a large number of *tax benefits*, which often inhibit the establishment of a competitive environment in the economy and facilitate the expansion of the informal economy. Thus a reconsideration of the existing benefits and abolishment of unjustified tax benefits will not only help create a competitive environment and equal opportunities for doing business, but will also replenish the state budget.

Another important direction in the reduction of transactional costs of doing business and improving the business environment and increasing the competitiveness of domestic producers, is **the reinforcement of ownership rights**.

It is important to mention that during the past few years, the government has paid a lot of attention to strengthening the legal protection of entrepreneurs. In particular, in 2005, the Decree of the President of the Republic of Uzbekistan On Measures to Further Improve the System of Legal Protection of Business Entities was adopted²⁵. The decree determines the conditions and procedures for interference of controlling bodies with the activities of business entities. In August 2006, the Law of the Republic of Uzbekistan On Arbitration was adopted, and regulates the establishment and operation of arbitration courts. The main benefits of arbitration compared with the standard judicial proceedings are their cost effectiveness, timely resolution of disputes, and opportunity to select the judges to resolve the disputes.

Despite the adopted measures, a number of problems in the area of protection of private property still remain. Based on numerous research, the most pressing problems in the protection of transactions and ownership rights include the following²⁶:

A. The legislation does not require reconciling draft laws, regulatory and legal acts, and other resolutions of state authorities and governance, which concern the interests of the private sector or certain market participants. Legislative acts contain a large number of indirect application regulations which require further details and references to subordinate departmental acts, providing extensive possibilities for rule-making to state authorities and governance bodies. As a result, the rules for doing business are not regulated by the legislative, but rather the executive branch of government, which contradicts the principle of separation of powers and is the main reason why the regulatory base is unstable, thereby impacting upon the investment climate in the country.

²⁵ For more details on the problems in protecting entrepreneur rights, see: "Improving Institutional Environment for the Protection of Ownership Rights in Uzbekistan, CER Report, 2006; "Improving Regulatory and Legal Base for Trade and Mediation Activities in the Domestic Market of Uzbekistan," CER Report, Tashkent, 2006; "Improving Regulatory and Legal Base of the Republic of Uzbekistan for Denationalization and Privatization," CER Report, Tashkent, 2006; Business Environment in Uzbekistan Through the Eyes of Small and Medium Business, Tashkent, IFC, Reports for 2003-2006; Uzbekistan: An Evaluation of Economic Development, Tashkent, World Bank, 2003.

²⁶ Pursuant to the Resolution of the Cabinet of Ministers of the Republic of Uzbekistan No. 109 dated 07.06.2006, On Improving State Duty System for Notary Actions.

The important direction is the reinforcement of ownership rights

The important direction is the reduction of administrative barriers for doing business

B. The lack of transparency and inconsistencies in legislation, as well as excessive restrictions on doing business, are also a threat to ownership rights. Lack of clarity in the legislation, a large number of unjustified restrictions and excessive requirements are a breeding ground for administrative pressure on business, and hence, a basis for high transactional costs. Such restrictions considerably worsen the competitive environment, and therefore reduce the efficiency of resource utilization and human development indices.

C. One of the main instruments in the protection of ownership rights and interests of entrepreneurs is *the judicial system*. Entrepreneurs experience the following problems:

- The imperfection of mechanisms guaranteeing equality of parties (prosecution and defense) in the course of a judicial proceeding;
- Insufficient qualification of court personnel due to the lack of specialized (tax and customs) courts;
- Red tape, protraction of cases and corruption in judicial bodies;
- Inefficiency of the mechanism for the execution of judgments, which sometimes leads to the protraction of execution for many months, and even years;
- The lack of independence of the judicial system from the executive power, and insufficient clarity of the distribution of authorities between the different branches of the government;
- High judicial costs restricting access to justice for private individuals and small private businesses.

The resolution of the above-mentioned problems and an improvement of the system of protecting ownership rights and of the judicial system may offer considerable support to the growth and development of productive business activities.

The third direction in the reduction of transactional costs of doing business and improvement of the competitiveness of domestic producers is the reduction of **administrative barriers for doing business: procedures for inspections, licensing, certification and standardization, etc.**

Administrative barriers for entrepreneurship often increase financial and time costs and limit the competitiveness of entities. With a view to reducing barriers and creating a favourable environment for business, a number of measures were taken by the government during recent years. In particular, the procedure for state registration of entities was considerably simplified with the discontinuing of the practice of complete due diligence of constitutive documents; while, internal procedures were also simplified. As a result, the 'one-window' registration with tax authorities and other state statistical bodies takes one day, saving entrepreneurs up to 16 days.

Furthermore, Uzbekistan increased the minimum term of business licenses from one year to five years. Licenses for 13 types of businesses in the areas of tourism, auditing, exchange, and professional stock exchange operations, have no validity terms.

The cost of transfer of ownership has also been considerably reduced, with

the state duty decreased from 10 percent of the value of property, to a duty based on the area of the property²⁷. This policy has made Uzbekistan one of the leading global reformers in ownership registration.

However, despite the adopted measures, administrative barriers for doing business are still significant. In particular, according to 'Doing Business 2009' Uzbekistan ranks 146th in terms of licensing problems, 170th in terms of obtaining a loan, and 119th in terms of ownership registration.

Existing administrative barriers include complicated procedures for obtaining permissions, approvals, licenses, certificates, standards²⁸; restrictions for trading in cash; and obstacles set by officials and law enforcement bodies while transporting and/or selling products to other districts and oblasts. In this context, in order to reduce costs of doing business and increase the competitiveness of enterprises, it is advisable to continue the further simplification of administrative barriers for conducting business.

5.1.4. Improving Foreign Exchange Policy

The foreign exchange policy is one of the major factors determining the investment climate in the country, the competitiveness of export items in global markets and of import-substituting items in the domestic market, and has a considerable effect on the prospects for modernizing the economy, as well as overall prospects for economic and human development. For this reason, the choice of the exchange regulations and a balanced foreign exchange market are one of the important conditions in achieving a competitive economy and sustainable long-term growth and development of the country.

Since 2002, the government's policy of unification of exchange rates of official and parallel exchange markets, and the introduction of free conversion for current accounts became an important factor in achieving high economic growth and an increase in exports. However, one of the consequences of the global financial crisis for Uzbekistan was the disruption of the exchange market balance and the emergence of a considerable gap between official and parallel exchange rates as a result of tightened exchange regulations for the purpose of maintaining the trade balance. Today, the US dollar exchange rate to the Soum in the parallel market is 40 percent higher than the official rate.

Persistence of this situation in the foreign exchange market may lead to a significant deterioration in the investment climate, reduced inflow of foreign direct investments into the processing industry, a drop in the competitiveness of export items, growth in illegal imports and corruption, and a reduction in proceeds from customs fees to the state budget. All of these could become a restricting factor for modernization, structural rebuilding of the economy, long-term growth and human development. For this reason, the most important priority in economic policy should be the improvement of the foreign exchange policy, and establishment and maintenance of a real exchange rate, at the level that supports the competitiveness of exports.

Effective foreign exchange policy contributes to the competitive economy and sustainable growth.

²⁷ Pursuant to the Resolution of the Cabinet of Ministers of the Republic of Uzbekistan No. 109 dated 07.06.2006, On Improving State Duty System for Notary Actions.

²⁸ These barriers were listed as the most problematic by 65.1% of respondents in a survey of managers of 1,500 non-state entities in all regions of Uzbekistan. The survey was based on a standardized interview and was conducted in 2006.

Overall, the adoption and application of a range of measures to develop the productive capacity of enterprises, to introduce international quality standards, to reduce transactional costs of doing business and to improve the foreign exchange policy can make a considerable contribution to the improved competitiveness of such enterprises and create appropriate conditions for formulating, and the efficient implementation of, a human development-oriented trade policy.

5.2. Improving the Quality of the Workforce and Human Development

Improving the quality of the workforce is an important factor in boosting the private sector's capacity for the production of competitive goods and creating the necessary conditions for the efficient implementation of the trade policy, and one of the main components of human development. This is the area, in which the interconnection between human development and foreign trade is most obvious.

Improvement of the education system, healthcare system and social infrastructure will contribute to human development

A well thought-through trade policy in a country producing goods that are competitive both in the domestic, and in international markets, creates opportunities to improve personal incomes and subsequently increase access to healthcare, education, and the necessary social infrastructure.

However, in order to produce goods that are competitive both in domestic and international markets, the workforce should have an appropriate level of education, access to necessary healthcare services, and be able to maintain appropriate living standards.

This interconnection illustrates the need for measures to be taken to build the capacity of human resources in order to increase the competitiveness of the economy, implement an effective trade policy aimed at long-term sustainable growth and high human development results in the country. In turn, the main directions in human development are the improvement of the education system, increased efficiency of the healthcare system, and development of the social infrastructure.

5.2.1. Improving the Education System

The level of education is one of the main factors influencing the quality and ability of the workforce to produce competitive goods. At the same time, the level of education is one of the main components of the human development index. In this context, the Government of Uzbekistan places high emphasis on reforms in the area of education. In particular, in 1996, the National Human Resources Training Programme was adopted for implementation until 2009; in 2004, the National Programme for School Education Development was adopted, also for the period until 2009. The enhancement of the education system is gaining increased importance today, as 2010 was named the *Year of Harmoniously Developed Generation in Uzbekistan*.

Increasing the quality of the workforce and human development in the country first of all means the need to improve the specialized secondary and higher education systems.

In order to create a holistic and continuous compulsory 12-year system of comprehensive and specialized vocational secondary education (SVSE), a teacher training and re-training base was created, and curricula and syllabi were approved in accordance with national educational standards. A wide range of additional measures was taken to make the transition to universal 12-year compulsory education during the 2009/2010 school year.

Currently, SVSE is provided on a full-time basis in two types of educational institutions: academic lyceums and vocational colleges. According to 2009 data, the country has built 1,335 SVSE institutions, educating 1,304,304 students, of which 1,208 are professional colleges with a headcount of 1,209,564 students, and 127 academic lyceums with a headcount of 94,740 students. The implementation of these measures led to significant improvements in the vocational secondary education numbers: during 2002-2007, the number of SVSE alumni per 10,000 of the population increased from 47 to 117.

In order to ensure the training of qualified personnel and employment of the alumni of specialized vocational secondary institutions, in 2005, the government adopted the '2006-2010 Standard Territorial Programme for Qualitative Training and Employment of Graduates of Vocational Colleges and Academic Lyceums', which provides for the creation of new jobs with financing from the off-budget Employment Fund. One of the results of the measures taken was a considerable increase in the share of employed graduates of specialized vocational secondary institutions: in 2007-2008, 92.1 percent of the total number of graduates were employed. However, the fact that only 46 percent of graduates were employed according to their specialization is also noteworthy. This indicates a problem with the mismatch between demand and supply in the job market, which is due to a number of reasons:

- The approach to the specialization of educational institutions, especially in rural areas, is characterized by insufficient flexibility in relation to changes in the job market²⁹;
- Vocational colleges provide education related to industrial professions in general, without a focused specialization in certain jobs, even during the last years of schooling, thereby limiting the opportunities for college graduates to start working at industrial enterprises without receiving additional training with a more focused specialization;
- The level of curricula and syllabi does not provide for the required level of education, as the secondary vocational education syllabi, in their majority, were compiled without consultations or coordination with employers.

In order to reconcile demand and supply in the job market, it is advisable to develop and regularly update the vocational education syllabi, based on the results of monitoring demand in the job market; to introduce multi-profile colleges, which would provide training in 10-15 key directions determined by the requirements of allied trades and specializations. Learning skills in several allied professions during three years of education will increase the likelihood of the employment of such SVSE graduates.

²⁹ For example, a specialized secondary education institution located in a certain area, which, year after year, graduates the same number of specialists for the same sector (for instance, kindergarteners and librarians). Amidst a relatively low mobility of the population, this leads to oversupply of the same profile specialists in some areas, and to their shortage in other areas.

Increasing the quality of the workforce means the need to improve the education system

A special importance is placed on higher education

Training of personnel for new industries, using the funds of initiators of investment projects, could play an important role in matching supply with the demand in the job market. For example, vocational colleges have been established to train personnel for oil and gas, chemical, and electric power industries, metallurgy, and road construction, with funding from major holding companies, entities and enterprises. A complete adaptation of syllabi of these educational institutions to the needs of specific sectors and enterprises could also contribute to the improvement in the quality of education, and a better orientation of the education towards the demands of the job market.

In the current globalized environment, with the development of information technologies and a transition to innovative development, there is a considerable growth in demand for highly qualified specialists, whose training falls beyond the capabilities of vocational secondary education. Therefore, a special importance is placed on *higher education* as essential in increasing the quality of the workforce, improving living standards and human development in general.

Higher education in Uzbekistan is represented by 69 higher educational institutions (including branches of foreign universities)³⁰, with higher education coverage constituting 109 persons per 10,000 of the population³¹. The quality of education is ensured through the introduction of state educational standards for 149 Bachelor degree courses and 650 Master degree specializations. These standards determine the requirements for the level of training, content and structure of the educational process. The gender profile of higher education institution students is 40.9 percent female and 59.1 percent male^{32, 33}.

With a view to improving the quality of higher education, a number of measures are currently being implemented, including the creation of the Higher Educational Institutions Development Fund, whose funds are used to create new textbooks, introduction of contemporary information technologies into the educational process, and modernization and refurbishment of educational buildings and dormitories. In addition to this, with the purpose of improving the efficiency of management and ensuring interconnection between universities, a common corporate and informational system was created, allowing the integration of all universities in the country into a common information system and introduction of elements of electronic document management. With the purpose of improving qualifications of promising young teachers and researchers, the network of teacher training institutions and programmes was expanded (including Iste'dod, the Fund of the President of RoU). The adoption of the aforementioned measures contributed to improved higher education figures: for example, during 2002-2007, the number of specialists with higher education per 10,000 of the population increased from 16 to 27.

However, despite the implemented measures and achieved results, the quality of

³⁰ Results are based on data presented on the official site of the Ministry of Education of the Republic of Uzbekistan (www.edu.uz).

³¹ Uzbekistan's Almanac -2008, CER, Tashkent, 2009.

³² According to 2006 data (source - http://statistics.uz/data_finder/2452/).

³³ In all likelihood, such gender inequality is due to a relatively early marriage age of most women (18-20 years) and gender stereotypes that especially exist in rural areas.

higher educational institution graduates does not correspond in full to the needs of the modern economy and requirements of employers³⁴. The government's and private sector's need for highly qualified personnel are far more dynamic than the capacity of educational institutions to satisfy such need. That is the reason why during the past few years the Republic is focusing on opening branches of a number of foreign higher educational institutions. Today, a number of educational institutions that were launched in cooperation with leading institutes and universities of foreign countries are operating in Uzbekistan³⁵. The emergence of these higher educational institutions created a competitive environment in higher education, which will play an important role, both in improving the quality of highly qualified specialists, and in matching supply in the educational market to the demand from employers.

At the same time, the current extensive state regulation and control in higher education does not allow for institutions' initiative, improvement of the quality of education, or an adequate response to the ever-changing demands of the labour market. For example, a complex and lengthy procedure for justifying the introduction of new courses, as well as a high share (90 percent) of compulsory³⁶ courses and disciplines, considerably restricts the attempts of the institutions to identify the needs of the labour market and target those in their operations.

In order to enhance the efficiency of higher education and improve the quality of the workforce, the medium-term development strategy provides for the following reforms in the higher education system:

Firstly, to identify new sources of funding, to develop competition, and, as a result, to improve the quality of higher education, it is advisable to create the necessary conditions for developing private education.

Secondly, in order to ensure the rapid response of universities to changes in labour market demands, it is suggested to reduce state regulation and promote the independence of universities by expanding their authority in the academic element, staffing, admission procedures and funding.

Thirdly, the mechanism of admission to higher educational institutions could be changed, to allow applicants to choose their specialization after tests, in accordance with passing acceptance scores in each institution. The budgetary funds in this case would be transferred to the institution that the applicant has chosen. This approach would promote competition between universities and subsequent improvement of the quality of education, which, in turn, will have a positive effect on the quality of the workforce and productive employment rates.

The adoption and implementation of the above measures and improvement of the educational system will, to a large extent, facilitate the improvement in the quality of secondary vocational and higher education, subsequent improvement of the quality of workforce, and, as a result, growth in productive employment and human development.

³⁴ In particular, according to the results of 2006 opinion poll among entrepreneurs, the level of economic major graduates is fully acceptable for 18.2% respondents, technical major graduates – for 18.6%, law major graduates – 17.0%, IT major graduates – 28.9%.

³⁵ These include Westminster International University, branches of Moscow State University, the I. M. Gubkin University of Oil and Gas in Russia, the G.V. Plekhanov Academy of Economics in Russia, Management Development Institute of Singapore, Turin Polytechnic University in Tashkent.

³⁶ Approved by the Ministry of Higher and Secondary Special Education.

5.2.2. Improving the Efficiency of the Healthcare System

An important factor of human development is improvement of healthcare system

An important factor in human development and improvement of the quality of workforce is the enhancement of the population's health and improvement of the healthcare system. In this context, from the 1990s, Uzbekistan has been conducting gradual reforms in the healthcare system. In particular, in 1998, the Healthcare Reform Programme was adopted, to be implemented until 2004. With the purpose of promoting maternal and children's health, the following programmes were adopted: Mother and Child Screening (1998), Healthy Generation (2000) and Protection of Motherhood and Childhood (2001). In line with global efforts to combat HIV/AIDS, the Government of Uzbekistan has developed a strategy for preventing the spread of HIV/AIDS for 2003-2006, and has set up the Emergency Anti-Epidemic Commission to coordinate preventative measures and treatment. In order to prevent socially dangerous diseases, the Strategic Programme for Reducing the Incidence and Prevention of Tuberculosis was adopted for the period of 2004-2008, providing for early detection of 70 percent and 85 percent recovery of tuberculosis patients. The state budget allocations for healthcare are continuously growing: in 2003, the share of healthcare expenses was 9.6 percent, but by 2007 it had increased to 11.6 percent.

The implementation of these programmes has resulted in improved health indicators for the population: during 2002-2007, the incidence of infectious diseases has decreased³⁷, drug- and substance-addiction cases reduced from 12.2 to 9.5 per 100,000 of the population, and active tuberculosis morbidity fell from 79.4 to 67.5 per 100,000 of the population. As a result, the mortality rate per 100,000 of the population decreased from 540.2 in 2002 to 509.7 in 2007, and infant mortality per 10,000 of the population decreased from 16.7 to 13.6.

Despite the numerous adopted and implemented programmes and achieved results, the current system of state financing of healthcare is not efficient. Although state funding of healthcare has increased, health indicators have not improved dynamically: for example, during 2003-2007, the number of infectious and parasitic disease incidents per 100,000 of the population only decreased by 4 percent, while maternal and infant mortality rates remained the same³⁸.

These numbers indicate the need to use the funding more efficiently and to create economic stimuli aiming to improve the quality of medical services and to develop the healthcare system. To resolve these problems, the following reforms are required in the healthcare system:

– Improving the healthcare state financing system through result-oriented budgeting mechanisms; improving the system of monitoring financial flows into healthcare;

³⁷ Namely, the number of incidents per 100,000 people of: acute gastrointestinal infections was reduced from 158.4 to 120.8; typhoid and paratyphoid fever dropped from 0.5 to 0.2; viral hepatitis dropped from 132.1 to 126.7; influenza from 3,173.9 to 2,037.1; and scarlatina, from 3.4 to 2.1.

³⁸ Maternal mortality per 100,000 live births remained the same at 32.3 during 2003-2007; infant mortality per 1,000 live births remained the same at 10.5 during 2003-2007.

- Enhancing the qualifications of medical workers according to international standards and introducing a system of certification and licensing that is more results-oriented;
- Improving management systems in healthcare by developing informational systems conforming to international standards;
- Introducing clinic audits as a measure to ensure quality, including certification and licensing of medical institutions for the purposes of efficient quality control in healthcare;
- Continuing the policy of creating and improving the facilities of modern highly technological, research-to-practice medical centres, which in most cases operate based on mixed funding.

5.2.3. Improving the Social Infrastructure

Human development is closely connected to the living standards of people. In turn, a considerable improvement in living standards could be triggered by the development of the social infrastructure and access to utilities. From 1990, Uzbekistan has implemented two state target programmes: to provide the population with clean drinking water and natural gas. As a result, as of the beginning of 2007, access of the population to central water distribution was 82.6 percent, and to natural gas, 81 percent.

The 2008-2010 medium-term country development strategy provides for the implementation of a number of programmes and measures to develop social infrastructure and to provide access for the population to utilities, including:

- Bringing central heating to 1,312 localities and construction of distribution networks to connect consumers;
- Reconstruction of 861.8 km of worn water supply networks;
- Replacement of 2,399 obsolete and inefficient boilers at social infrastructure sites with modern energy-saving boilers in schools, hospitals, etc.
- Reconstruction of 515 km of worn heat supply networks;
- Implementation of 17 projects worth US\$ 600 million to increase the clean drinking water supply.

Further development of the social infrastructure involves:

- Improving management and control systems, increasing the responsibility of utility companies for uninterrupted supply of the population with utilities;
- Introducing a mechanism of raising long-term funding to develop city engineering and utility infrastructure, using various sources;
- Improving tariff policies by setting tariffs for utilities based on cost, required profits and taking into account the population's capacity to pay;
- Improving housing and utilities infrastructure maintenance and repair systems, by improving physical facilities and attracting investments for their development;
- Ensuring rational usage of resources and conservation of energy resources;
- Developing regional programmes to deepen economic reforms in utility services.

The implementation of the measures listed above will promote human

Improvement in living standards could be triggered by development of social infrastructure

development both directly and indirectly – through the improvement of the quality of workforce, subsequent improvement of the competitiveness of the economy and creation of conditions for an effective trade policy targeting human development.

5.3. Developing a Strategic Trade Policy

The current export regime (see Box 5) and implementation of economic policy measures during the last few years have facilitated the achievement of high export growth rates, which became an important factor in accelerating economic growth and real personal incomes.

Box 5. Export Regime of Uzbekistan

The Republic of Uzbekistan's foreign trade regime exhibits openness, where **exports** are concerned. For example, export customs duties are not applied in the Republic; export of goods (works and services) for hard currency, including supplies to CIS countries, are taxed at zero VAT; and exports of goods by producers is exempt from excise tax, except certain excisable items as determined by the Cabinet of Ministers. There is no quantitative restrictions (quotas) or licensing (except for specific goods¹) for exports. A number of important preferences are provided under the Anti-Crisis Programme (see Section 4.2) to support exporting enterprises.

¹ Appendix No.1 to the Decree of the President of the Republic of Uzbekistan No.UP-1871 dated 10.10.1997 approved the list of specific items, whose exports and imports shall be implemented under licenses issued by MFERIT, based on resolutions of the Cabinet of Ministers. The list includes armaments and military equipment, including components used in their production, precious metals, alloys and items made of the same, uranium and other radioactive materials and their products, radioactive waste, devices and equipment using radioactive materials.

Development and implementation of trade policy strategy will contribute to human development

However, the share of commodities in total exports of the country is still considerable (approximately two-thirds), which results in a high dependence on volatile global prices for commodities and poses a threat to the sustainability of the long-term economic growth and achievement of significant human development results. For this reason, an important condition for increasing the role of the trade policy in human development, along with creating and building the government's and private sector's capacity, is to develop and implement **a trade policy strategy**, targeting high economic and human development results in the long run. Such a strategy should become the basis for measures to improve the trade policy in the short-, medium-, and long-term.

The strategic goal behind improving **the export regime** is to reduce the share of commodities and increase the share of finished goods in its structure, in order to reduce the consequences on the macroeconomic level, and that of employment and personal incomes, from volatile global prices for commodities, and to ensure the sustainability of long-term economic growth with a view to achieving significant human development results.

Stimulating exports of non-commodity items, especially in labour-intensive industries, can facilitate the creation of efficient jobs, an increase in real

personal incomes and reduction of poverty, and, as a result, the achievement of high human development results. In addition to this, increased exports of finished goods do not only lead to increased revenues for exporters, but also to positive effects for the entire economy. Namely, in most cases, the production of non-commodity items adds high value addition, and involves a long chain of subcontractors and associated services. This means additional jobs both in export-oriented and in other related sectors of the economy. As additional jobs in the production of finished goods often have higher requirements in terms of the qualifications of the labour force, it will also promote the improvement of its workers' qualifications.

The improvement of the country's **export regime** could become one of the factors stimulating non-commodity exports with high value addition.

As illustrated by the results of an opinion poll of entities participating in foreign economic activities⁴⁰ and an analysis of the current regulatory and legal base, an entity involved in foreign trade in Uzbekistan has to go through a lengthy and complicated process, while in the process of carrying out foreign economic activities, exporters bear high transactional costs.

According to the World Bank, the average time for exporting procedures in Uzbekistan is 44 days, which is high, particularly in comparison with foreign practices: for instance, in Denmark and Estonia, export procedures take only five days, while in Belgium, Canada, Germany and Switzerland, it is seven days⁴¹.

To reduce the total time spent on foreign trade operations in Uzbekistan, the number of bureaucratic procedures needs to be reduced, while the regulations for such transactions have to be improved.

The main problems that arise during the process of exporting, on an individual procedural basis, are as follows:

- Procedure for *the certification of origin of goods*. Pursuant to existing regulations⁴², inspection of the origin of goods and printing of the certificate takes three business days from the date of application, submitted in an established manner. In the case of additional information on the origin of goods being required, the application turnaround time could be extended by up to six business days. Thus, it is advisable to terminate the authority to extend the origin inspection time, in order to prevent potential deliberate delays by experts of the authorized agency, as well as to determine an exhaustive list of documents required for such inspection.

³⁹ Appendix No.1 to the Decree of the President of the Republic of Uzbekistan No.UP-1871 dated 10.10.1997 approved the list of specific items, whose exports and imports shall be implemented under licenses issued by MFERIT, based on resolutions of the Cabinet of Ministers. The list includes armaments and military equipment, including components used in their production, precious metals, alloys and items made of the same, uranium and other radioactive materials and their products, radioactive waste, devices and equipment using radioactive materials.

⁴⁰ Report on the Results of Survey on Current System of Export-Import Operations and Customs Administration; UNDP, 2007, Tashkent.

⁴¹ According to the World Bank – Doing Business 2009. Source: www.doingbusiness.org.

⁴² Clause 2.1. Statute on the Procedure of Certifying the Origin of Goods in the Republic of Uzbekistan, registered with the Ministry of Justice under No. 945, dated 13.07.2000.

Stimulation of exports of non-commodity terms, especially in labour-intensive industries, will contribute to the productive employment

Optimization of import regime will improve the population welfare

- *Export customs formalities.* Pursuant to Article 76 of the Customs Code, customs declaration of goods and vehicles is implemented by a customs body not later than within ten days from the date the customs declaration is received and all necessary documents and information are presented. Compared to other countries, customs declaration of goods in Uzbekistan is a rather lengthy process (for example, in Russia it takes only three days). In terms of simplifying customs formalities, it is advisable to: a) cancel the procedure of contract registration with customs authorities, as the same can be undertaken during other customs formalities; b) reduce the number of stages in customs declaration from five to three, by combining the stage of accepting and registering of Cargo Customs Declarations (CCD) with the stage of checking the correctness of TNVED⁴³ (customs) codes, and the stage of checking customs value with the stage of verifying customs duties.
- *Timeframe for hard currency proceeds.* Pursuant to the effective legislation⁴⁴, if hard currency proceeds are delayed by more than 30 banking days (in 2009, as part of anti-crisis measures, this timeframe was extended to 60 banking days⁴⁵), resident legal entities must pay a penalty to the national budget for the sum of 100 percent of the outstanding amount. According to a survey of domestic exporters, the 30-day timeframe for receiving hard currency that was effective before the financial crisis, was not sufficient for export operations, and therefore could be restricting the growth and development of exports in the country. In this context, it is advisable to reclassify the measures to extend the period after which penalties are exercised from 30 to 60 days, that were adopted within the Anti-Crisis Programme, from being temporary to permanent, and to introduce gradual penalties for the delay in hard currency proceeds. It is also necessary to permit exporters to pay tax liabilities within an established timeframe and sell currency proceeds, using any other available assets, without application of sanctions against the same⁴⁶.

The development of export potential and an increase in the exports of non-commodity items with high value addition could also benefit from the extensive involvement of intermediary companies in export activities. The experiences of foreign countries indicates that the involvement of intermediary organizations in exports is often more efficient (as it involves lower costs), than if exports are done by the producers themselves.

Presently, participation of intermediary entities in export activities in Uzbekistan is insufficient, due primarily to their inability to obtain a number of benefits and preferences in terms of taxes and customs duties, while manufacturing companies enjoy such benefits.

⁴³ TNVED is the coding for export-import operations used in CIS countries.

⁴⁴ Resolution of the Cabinet of Ministers No.245 dated 29.06.2000, On Measures for Further Development and Consolidation of Over-The-Counter Currency Market.

⁴⁵ Pursuant to the Decree of the President of the Republic of Uzbekistan No.UP-4058, dated 28.11.2008, On the Programme of Measures to Support Entities of the Real Sector of the Economy, to Ensure Their Stable Operations and to Increase Export Potential.

⁴⁶ Analytical Note, Foreign Trade Regime of Uzbekistan and Main Directions in its Improvement, CER, Tashkent, 2009.

In this regard, it is advisable to create a system of incentives for intermediary companies, including the extension of *benefits and preferences that are granted to exporters of own products*.

The ultimate goal of developing and implementing the strategy of the import regime is to ensure a more efficient distribution and utilization of resources in order to achieve sustainable economic growth and improvements in the nation's welfare.

Today, the country's **import regime** is characterized by a high level of protectionism, in the form of high customs fees, which, in addition to customs duties, include value-added tax and excise taxes for imported goods (see Box 6).

Box 6. Import Regime of Uzbekistan

The Republic of Uzbekistan uses ad valorem and complex customs duties with respect to 97 commodity groups at rates varying between 0 and 30 percent. The arithmetic mean customs tariff is 14.88 percent.

Excise taxes are applied to imports of 51 commodity groups, with excise tax rates varying on average between 5 percent and 70 percent¹.

Imported items are also taxed with value-added tax at 20 percent². Furthermore, the value-added tax is charged based on customs value of the goods plus customs duties and excise taxes.

The existing import regime has a number of undesirable side effects

¹ Exceptions are: water, natural, mineral or sparkling (100%), carpets (90%), jewelry (140%), and ice-cream (100%).

² Exempt from VAT are imports of technological equipment brought to equip priority objects included in the investment programme, to implement investment projects financed from foreign loans guaranteed by the government, and for newly built enterprises to produce consumer goods.

According to estimates, an average level of established customs fees, calculated at the ratio of accrued customs fees (customs duties, excise tax and VAT) to the value of imported goods, constitutes 40.9 percent⁴⁷.

At the same time, the average rate of actually paid customs fees on all commodity groups is 8 percent, which is nearly 5 times less than the average official customs fee⁴⁸. This is attributed to the fact that a large number of benefits are used with respect to imports by certain enterprises and for certain industries.

A considerable increase in customs fees occurred during the introduction of free conversion of Soum under current operations, with the purpose of reducing demand for imports and preventing a slump in the Soum exchange rate⁴⁹. These measures allowed for liberalizing the currency market without a significant reduction in the exchange rate, which played a vital role in preventing an international loan crisis in the real sector of the economy.

However, the existing import regime has a number of undesirable side

⁴⁷ Analytical Note, Foreign Trade Regime of Uzbekistan and Main Directions in its Improvement, CER, Tashkent, 2009.

⁴⁸ Actual rate in this case means an average size of actually paid customs fees weighted versus the actual value of imported goods.

⁴⁹ Prior to the introduction of conversion under current operations, the main instrument of the protectionist policy was currency control.

effects, which will have a negative effect on the prospects for economic and human development in the long-term.

Firstly, the application of a protectionist regime with respect to certain items became the reason for a sizeable distortion of relative prices, which, in turn, creates inefficient distribution and utilization of resources and is the reason for a diminishing in the nation's welfare. Distorted prices give entrepreneurs false ideas on the utilization of resources and decrease the benefits of participation in the international labour market. The persistence of this situation in the medium- and long-term could lead to considerable structural costs, as investment decisions made amidst distorted prices could prove inefficient upon liberalization of the foreign economic activities.

Secondly, the application of protectionist measures has a negative impact on the growth of export capacity due to the overstatement of the real exchange rate, appreciation of components and raw materials used in the production of export items and outflow of resources from import substitution.

Thirdly, trade protectionism leads to an increased monopolization in the economy and restrictions of the competitive environment. This is confirmed by the fact that the concentration in commodity markets that are most protected by customs fees, is high⁵⁰. Although for a number of these items, actual customs fees are lower than the established ones (because of the practice of granting preferences to certain enterprises): this does not solve the problem, but rather creates the conditions for violating the principle of fair competition and economic monopolization.

Granting preferences on import customs fees to certain enterprises with a view to supporting priority industries places such enterprises in an advantageous position compared with other enterprises operating in the industry, and increases the risk of monopolization of the respective commodity markets. However, the existing system of benefits reduces incentives for business entities to invest in the localization of production, and expand the assortment and volumes of domestic production, as often imports – including all of the benefits granted to specific enterprises – bring more profit than domestic production.

Fourthly, high import customs fees stimulate contraband imports, which result in the reduced efficiency of measures to protect domestic producers.

The need to resolve the aforementioned problems, as well as the specifics of the current situation in domestic and external markets indicate the need to optimize the existing import regime. However, a sudden and full-scale liberalization of the import regime could lead to considerable structural costs and have a significant negative impact on the welfare of the population. Therefore, in order to minimize the structural costs for national producers to adapt to new conditions and to prevent a sudden deterioration in the population's welfare, it is advisable to develop a **Programme for Import Regime Optimization**. Such a programme should provide for a gradual reduction of import barriers given the existing situation in a specific industry, creation of conditions for competition and breaking the monopoly power by abolishing unjustified benefits in terms of customs payments. Such a programme, together

⁵⁰ Analytical Note, Impact of Customs Policy on the Monopolization of Economy for Certain Goods, CER, Tashkent, 2006.

There is a need to develop a Programme for Import Regime Optimization

with the gradual nature of the liberalization of the import regime, will allow national producers to prepare for and ensure maximum efficiency in the new conditions. The liberalization of the import regime should be accompanied by a reduction in the real exchange rate of the national currency, with the purpose of stimulating exports, restricting imports and preventing a sudden decline in the trade balance. Such a policy would promote overall efficiency of the economy as a result of reduced distortions in relative prices and more efficient distribution and utilization of resources, which is an important condition for human development in the medium- and long-terms.

Another direction in the optimization of the import regime are measures taken to reduce transactional costs of import operations by simplifying customs procedures.

The results of a World Bank survey indicate that the total average time for compulsory procedures related to items imported into Uzbekistan is 92 days⁵¹, a figure which is one of the highest in global practice.

The presence of considerable and costly barriers for importers means a high cost of import transactions, resulting in inflated prices for imported goods in Uzbekistan, and also increased smuggling and corruption in state bodies.

According to the results of a survey of domestic importers, the main challenges related to importing are:

- Pursuant to Article 76 of the Customs Code, customs declaration of goods and vehicles is implemented by a customs body no later than ten days from the date the customs declaration is received and all necessary documents and information are presented. This period is unnecessarily long and increases transactional costs for importers, including in the storage of goods in bonded warehouses.
- The requirement for a preliminary inspection of import contracts by Ministry for Foreign Economic Relations, Investment and Trade increases transactional costs of import operations. Pursuant to the effective regulations⁵² the following import contracts are subject to MFERIT inspection: 1) financed from state budget; 2) financed from loans (borrowings), raised by the Government of Uzbekistan or under its guarantee; and 3) executed by business entities, whose charter capital has a state share exceeding 50 percent, and lacking own hard currency assets. It appears that the improvement of the system to determine the customs value of imported goods in accordance with the norms of the treaty to join Article VII of WTO will create the conditions for abolishing this requirement. The provisions of the new draft of the Customs Code currently in development takes these international norms into account.
- An analysis of compulsory import procedures showed that most of the stages are too complex. In this context, similarly to the proposed measures on simplifying export procedures, it is advisable during the first stage, to:
 - ◊ Discontinue contract registration with customs authorities, as the same can be done during implementation of other customs formalities;

The presence of considerable and costly barriers for importers means a high cost of import transactions

⁵¹ According to the World Bank ('Doing Business 2009').

⁵² Decree of the President of the Republic of Uzbekistan No.UP-3321 dated 26.09.2003.

The procedures and conditions of customs formalities and customs control should be clear and transparent

- ◇ Reduce the number of stages in the customs declaration from the current five to three, by combining the stage of accepting and registering of CCD's with the stage of checking the correctness of TNVED (customs) codes; and the stage of checking customs value with the stage of verifying customs duties.

The amending of the current customs administration is an important factor in creating favourable conditions for foreign economic activities, and, hence, establishing a favourable business climate in the Republic of Uzbekistan. A new edition of the Customs Code has been developed, which should become a direct action act. The draft is synchronized with the provisions of the International Convention on the Simplification and Harmonization of Customs Procedures, customs codes of the European Union, member states of EurAsEC, effective legislation of Uzbekistan, the Tax Code and draft Code on Administrative Liability.

The main additions to the new draft of the Customs Code are:

- ◇ Introduction of a risk management system;
- ◇ Establishing measures to protect intellectual property rights and determining the role of customs authorities in their implementation;
- ◇ Regulation of application of information systems, information technologies and their support;
- ◇ Introduction of provisions on notifying and consulting on customs matters, and setting specific timeframes, locations and time for providing such notifications or consultations.

The transition to the new system of organizing customs control and customs formalities will enable an optimal correlation between the time spent on customs control and its efficiency, and will ensure the swift completion of customs declaration of goods and vehicles, transported through the borders. This should become a key element in improving customs administration system. The procedures and conditions of customs formalities and customs control should be as clear and 'transparent' as possible, and have a common information space, and efficient information, technical, and legal support.

To implement the set tasks, efforts need to be focused on major directions in simplifying foreign trade procedures and upgrading the customs system, including:

- ◇ *Introduction of a 'One Window' mechanism*, which would allow the parties participating in trading and shipping operations to present standardized information and documents using a single channel to complete all regulatory requirements concerning imports, exports and transit;
- ◇ *Introduction of preliminary and electronic declaration*, which would allow for the documentary audit of information presented in CCD prior to actual presentation of the goods to the customs body;
- ◇ *Introduction of a risk analysis and management system*;
- ◇ *Introduction of a post-customs control system*, which provides for the completion of all customs controls after the release of the

goods (completion of the bulk of customs formalities), not during the declaration or preliminary operations, so that shipments are not held at customs; and inspection is based on presented documents;

- ◇ *Harmonization of declaration forms with international standards* (by introducing a Single Administrative Document⁵³), which primarily aims to improve the procedure for declaring goods moved through a customs border and to unify customs documents. This would allow harmonizing customs formalities with those of the European Union, simplifying customs procedures and accelerating customs clearance.

It is expected that the implementation of the above recommendations and adoption of the new edition of the Customs Code will allow for considerable simplification of procedures related to foreign economic activities.

The implementation of the aforementioned measures and optimization of the foreign trade regime will promote the creation of a competitive environment, reduce pricing distortions, increase export potential and opportunities for growth in employment and incomes, and, as a result, improve human development indices in the country.

5.4. Agricultural Sector Reform and Stimulating Employment

Uzbekistan has a large labour supply, a relatively high level of education and a relative cheapness of the labour force. Subsequently, while developing trade policy, special attention must be paid to the development of labour-intensive industries, producing non-commodity goods with a high value addition (Box 7).

Box 7. Stimulation of employment

Creating a more dynamic process of urbanization and reducing urban poverty will have to go hand-in-hand with an industrial strategy that is more employment-oriented. Such a strategy could encompass a variety of measures, which could include explicitly channeling public investment and resources into internationally competitive employment-intensive sectors. Such measures could also involve the use of tax and subsidies and commercial credit to promote priority sectors or the use of public sector matching funds for approved private-sector investment projects.

Currently, a comprehensive Master Plan of Population Settlement is being prepared by the Cabinet of Ministers in Uzbekistan, but its recommendations are not vitally linked to projections of industrial growth and employment generation, which would be crucial for realistic planning of the urbanization process. We thus recommend that, while striving to develop a more comprehensive and coherent industrial policy, the government of Uzbekistan focus on linking that policy to a well-articulated master plan for urban development. This includes the generation of widespread and remunerative employment, which can support increases in private incomes and public financial resources. It would also entail the spreading of such employment opportunities outside the Tashkent area in order to create more balanced and sustainable industrial and urban development.

«Addressing urban poverty in Uzbekistan in the context of the economic crisis», ЦЭИ, 2010

⁵³ Foreign trade of Uzbekistan with countries using SAD (mainly, EU countries and Russia) at the end of 2006 constituted 38.4%.

An important factor of ensuring successful agricultural reform is improvement of the efficiency of land utilization

However, in order to ensure sustainable development in the long run, priority industries have to be determined which are not based solely on supply factors, but also take into account global trends, in terms of demand (i.e. an industry's products should be potentially competitive in international markets).

Stimulation and development of labour-intensive industries, in which the majority of employees are female (for example, textile and apparel), will not only facilitate a growth in employment, incomes and living standards, but will also help to resolve the gender inequality issue.

In order to ensure gender equality, the government has taken special measures to stimulate employment among women. In particular, local authorities organize jobs for women and allocate special funds to train women in different professions. Non-government organizations (NGOs) also play a major role in the creation of jobs, including Women Committee, Association of Business Women, Association of Women NGOs, etc.

However, despite the measures adopted to achieve gender equality, according to 2007 data, the share of women in the total employed population constituted of 46 percent. The stimulation of labour-intensive industries, where women represent the majority of those employed, would promote gender equality, in terms of employment and incomes.

The issue of gender equality in many ways determines the living standards and quality of life of the population, the social climate in the country, the implementation of the principle of equal rights and freedoms, the creation of equal opportunities for all members of the society, and henceforth, the welfare of the overall society.

Another potential direction in ensuring employment and growth in personal incomes is through incentivizing the development of the agro-industrial complex. Presently, over 60 percent⁵⁴ of the population lives in rural areas, and nearly 30 percent⁵⁵ are engaged in agriculture. It is also important to develop agriculture to provide food security and access of the population to food (see Box 8).

In order to increase the efficiency of agricultural production and its physical infrastructure, structural reforms in the form of consolidation of farms are being presently implemented in the agricultural sector⁵⁶. The consequences of these reforms are somewhat contradictory: on the one hand, they may result in increased productivity and competitiveness of the agricultural sector, but on the other hand, could lead to a sudden increase in the supply of labour and a reduction in employment in rural areas. For example, as a result of consolidation in the agricultural sector during October 2008 – January 2009, only 105,000 farms remained of 220,000 farms, and over 115,000 farmers (over half-a-million individuals including family members) lost the land plots which they received during the previous stage of agricultural reform. CER estimates⁵⁷ that the growth in productivity of the agricultural sector resulting from the consolidation of farms will be associated with a drop in employment from three

⁵⁴ 62.2% according to 2008 data.

⁵⁵ 27.7% according to 2008 data.

⁵⁶ Consolidation of farms means merging several small or medium private farms to create one private farm with a large land plot.

⁵⁷ Urbanization and Industrialization in Uzbekistan: Challenges, Problems and Prospects, Analytical Note, CER, 2009/01.

Box 8. Sustainable agriculture and food security in Uzbekistan

At the moment The Center for Economic Research develops the Concept on the National policy for Sustainable Agriculture, Food Security and Nutrition. The key goal of the concept is Facilitating balanced public nutrition as a key factor of public health and nurturing the physical and intellectual development of the nation.

The main hypothesis of the concept is that the problem of the balanced nutrition in the conditions of Uzbekistan should be solved by focusing on the three following aspects:

1. Increasing public awareness about safe and healthy nutrition according to developed nutrition standards;
2. Ensure that households have access to nutritious food;
3. Creation of effective legislative system for ensuring food quality and standards.

Based on the Concept the logframe of goals was developed.

Logframe of Goals National Policy for Sustainable Agriculture, Food Security and Nutrition

Main goals	Activities for Achievement of Objectives	Instruments and Specific Measures taken in each Area
1. Increasing public awareness about safe and healthy nutrition according to developed nutrition standards	1.1. Evidence-based nutrition standards developed for each gender and age group taking into account the natural and cultural environment in Uzbekistan	1.1.1. The institutions responsible for the development and systematic improvement of nutrition standards and the monitoring of actual intake including for vulnerable groups as defined by legislation (particularly infants and young children, pregnant and breastfeeding women and the elderly) and the development of innovative approaches to nutrition and food safety issues. 1.1.2. The system of statistical surveys of the food consumption by different gender and age groups, along with the accessibility of foodstuffs, particularly for vulnerable groups, improved
	1.2. Effective system of public awareness and disclosure of information on healthy and safe nutrition based on the principles of healthy nutrition created	1.2.1. The system of observations of the relationship between the morbidity rate and level and structure of consumption of food at the medical institutions is improved. 1.2.2. Systematic media publications along with brochures and books on the principles of safe and healthy nutrition organized 1.2.3. A special website with regularly updated information and free counseling by doctors and nutrition specialists on the principles of healthy and safe nutrition launched
2. Ensure that households have access to nutritious food	2.1. Enabling environment for receiving the income sufficient for purchasing essential foodstuffs according to the approved standards created. Poverty rate is reduced and access of vulnerable groups to foodstuffs is significantly improved	2.1.1. Government bodies create a favorable economic and financial environment such that economic growth results in increased employment and income, primarily for poor households through various programs of support to the poor and other socially vulnerable households 2.1.2. Government support to more rational structure of consumption (nutrition) of the poor and the most vulnerable groups of population provided 2.1.3. A system to prevent price fluctuations for major foodstuffs introduced
	2.2. Effective agricultural production of foodstuffs organized to ensure sufficient output for domestic demand and exports to maintain the income of rural households	2.2.1. Optimal cropping patterns developed and maintained to ensure soil conservation and productivity 2.2.2. The system for effective utilization of land and water resources to maintain crop yields created and maintained 2.2.3. System for improving the agricultural skills of farmers created 2.2.4. State support for the development and implementation of innovations to improve agricultural efficiency in place 2.2.5. Government support programme for greenhouse-based crop cultivation without the use of natural gas developed and widely implemented 2.2.6. Programme of compound feed production for the development of livestock and poultry farming developed and implemented 2.2.7. International experience of high-breed livestock, poultry, field crops, fruits and vegetables farming widely used 2.2.8. A programme the for expansion of fish farming developed and implemented

Main goals	Activities for Achievement of Objectives	Instruments and Specific Measures taken in each Area
2. Ensure that households have access to nutritious food	2.3. Creation of an effective system for the procurement, storage, and industrial processing of agricultural raw materials	<p>2.3.1. All restrictions to access to cash for the procurement of agricultural produce by specialized procurement, trade and food processing companies and other wholesale buyers of fruits and vegetables as well as dairy and livestock products eliminated</p> <p>2.3.2. Unrestricted access of procurement and food processing companies, trade businesses and special trade associations to bank loans facilitated</p> <p>2.3.3. System of future contracts to procure agricultural produce by procurement and food processing companies implemented including orders for specific varieties of fruits and vegetables or production of cattle and poultry breeds with certain quality features and volumes</p> <p>2.3.4. A system of bank loans to generate food supplies by farmers and private procurement companies created, particularly for winter storage and the subsequent sales of fresh fruits and vegetables to households in winter.</p>
3. Creation of effective legislative system for ensuring food quality and standards	2.4. Creation and effective use of state food reserves 3.1. Development and enforcement of standards for producers, processors, and sellers of foodstuffs	<p>2.4.1. Mechanism to ensure timely adjustment of state strategic reserves and private food reserves according to changing circumstances</p> <p>3.1.1. Internationally tested system of quality control for foodstuffs from production to sale gradually created, according to the "From farm to fork" principle, and an intersectoral system of food safety and mechanisms for risk analysis established with annual reviews of progress in the achievement of internationally recognized standards</p> <p>3.1.2. Legal liability for violations of established quality standards in the production of food products developed based on objective criteria by increasing the fine in cases of repeat offences up to closure of businesses in cases when offences were not remedied.</p> <p>3.1.3. Regulations banning the advertisement of unhealthy or harmful products (prohibiting advertising tobacco and alcoholic beverages near educational institutions), and liability for offences established.</p>

to two million. Thus, there is a strong need to minimize the negative social and economic consequences of agricultural reform by pursuing policies aiming at growth in employment and personal incomes in rural areas.

An important factor in ensuring successful agricultural reform and improved welfare for the rural population is the improved efficiency of land utilization. Land in Uzbekistan is the main means for production and source of income for most of its rural population. Each hectare of irrigated agricultural lands serves an average of 8.2 people, while population growth rates exceed the rate of increasing irrigated lands. However, an individual employed in agriculture provides for an average of six-to-eight times less people than in developed countries. Therefore, further economic and human development of the country is closely tied with increased efficiency in utilizing agricultural lands. To achieve this goal, implementation of the following measures is recommended:

At the governmental level:

- Introduction of amendments and changes to the Law on Land, in order to develop a system of fair relationships between administrators and users of land resources in relation to issues of land usage, volume of government contracts, and distribution of responsibility between the government and land users in terms of financing irrigation, melioration, chemicalization and land treatment and usage;

- Development of medium- and long-term programmes to support and develop major water agencies involved in irrigation and melioration;

- Support to agricultural producers in terms of provision of information on agricultural techniques, innovative developments, structure of production and demand for agricultural products;

- Incentivization for the introduction of water-saving production technologies in the agricultural sector;

- Incentivization for the establishment of agro-industrial firms with a view to further process and export horticultural and agricultural products.

At the level of private farms and dehqan entities:

- Development and implementation of medium-term programmes to support and improve the fertility of soil on rented plots;

- Introduction of innovative methods for soil cultivation, sowing and irrigation.

Another important factor concerning the growth in real incomes of the rural population is the incentivization of production and exports of horticultural products. Approximately 20,000 farms and several million dehqan entities harvest fruits and vegetables, and a stable growth in the production and exports of horticultural produce in the medium-term could become a major factor in increasing the incomes of rural citizens.

Total annual production of fresh horticultural produce exceeds six million tons. However, production capacity, and in particular, the capacity for exporting fresh horticultural produce is not sufficiently utilized: despite the variety and palatability, only 10-11 percent of Uzbekistan's produce is exported.

The main measures aimed at stimulating production and export of horticultural products include:

- Discontinued sowing of cotton and wheat on lands that do not provide economically viable harvests of these crops;
- Replacing bans on export of horticultural products with the introduction of temporary export customs duties during sudden increases in prices in the domestic market;
- Increasing state financing and improving efficiency of seed development and wine growing research institutes through their integration within the production, and by creating economic stimuli for the end results in their activities;
- Creating an efficient system for certifying agricultural products;
- Stimulating the creation of large agro-industrial firms through vertical integration of processing and agricultural enterprises;
- Stimulating the creation of intermediary trading firms or farm cooperatives to sell produce domestically and internationally.

The implementation of measures aiming to stimulate growth in the production and exports in labour-intensive industries, as well as measures to develop the agricultural sector of the economy, can facilitate growth in employment and improvement in the welfare of rural and urban populations, and ensure efficiency in the implemented trade policy as a factor in achieving positive results in terms of public welfare.

The main condition for human development in Uzbekistan is the development of the transport infrastructure

5.5. Developing the Transit and Transport Infrastructure

One of the main conditions for realizing the potential of a trade policy aiming for long-term growth and human development in Uzbekistan is the development of the transport infrastructure. The transport industry plays an important role in stimulating economic activity, expanding sales markets, ensuring access of economic agents to resources, and is one of the principal factors of a successful integration of the country into the global economy. An inefficient transport system can be associated with high costs in production and services, and exports and imports, with a reduction in the competitiveness of local producers and a respective decrease in the population's welfare. The development of the transport infrastructure is of major importance for Uzbekistan, given that it is a landlocked country.

Uzbekistan has a high transit potential, especially considering from a regional perspective, due to its central location in relation to other Central Asian countries, thereby making it the most optimal 'bridge' connecting Central Asian countries with each other and providing access to other regions. The close ties between CIS economies, the considerable interdependence of their markets and the well-functioning transportation and communication infrastructure are additional factors, contributing to the transit capacity of the country.

Since independence, Uzbekistan has been developing its transport infrastructure: during 1991-2007, the total working mileage of railway track increased from 40,500 km to 49,100 km; highways, from 10,500 km to 13,400 km; with cargo turnover increasing from 38.4 billion ton-km in 1997 to 61.1 billion ton-km in 2007. The establishment of the Navoi free industrial economic

zone is another significant development. The management of the newly built Navoi airport was transferred to an international operator (Korea's Korean Air) and a transcontinental multi-modal logistics centre was set up. This will enable a reduction of up to three times in the distance of international air carriage from South and South-East Asia to Europe and North America.

Despite the achieved results, the burden of transportation costs in export and import operations remains high. For example, other than the export of certain commodities and imports of heavy machinery and equipment, transportation charges represent 16-19 percent of the total value of the country's exports and imports. In comparison, the share of transportation costs for Asian countries generally constituted 8.1 percent of total volume of foreign trade operations, while the global average is 6.1 percent.

With a view to developing the transport sector and reducing transportation costs in export-import operations, the following measures are being implemented:

1. Developing alternative transportation corridors:

– Implementation of projects to develop the Dostyk-Alashankou-Urumqi rail route, to engineer the Andijan-Osh-Kashgar highway, and to design and construct the Hairaton-Mazar-i-Sharif-Heart railway line;

– Continuing pilot air shipments within the Navoi Transport Initiative, and simultaneous construction and reconstruction of the E-40 road transport corridor;

– Active participation within the Working Group under the Ministers Meeting of SCO state members, responsible for foreign economic relations on the construction of the E-40 transport corridor segments;

– Consider executing an interdepartmental agreement on cooperation in the area of railroad transportation between Uzbekistan Temir Yullari SJSRC and Turkish Railway.

2. Increasing exports of transportation and transit services:

– Re-orient a considerable share of trade flows between Europe and Asia to domestic transit routes by increasing the competitiveness and attractiveness of transport corridors of Uzbekistan;

– Organize logistics centres based on the existing infrastructure in the main cargo-generating and cargo-consuming regions of the Republic and in the major transportation hubs at the intersection of main international transport corridors;

– Expand opportunities for the transcontinental logistics centre in Navoi city airport, by:

- ◊ commissioning a cargo terminal with a capacity of 300 tons/day and centralized refueling system with a 400 cubic meter oil tank;
- ◊ attracting transnational logistics companies to use the services of the cargo terminal;
- ◊ increasing the number of Korean Air flights transiting between South-East Asia and Europe, and attracting additional volumes of cargo and passengers;

- ◇ expanding the geography of international flights by Uzbekistan Havo Yullari NAC, by launching new international routes to CIS and former Soviet countries, and attracting foreign air companies to use the services of Navoi airport;

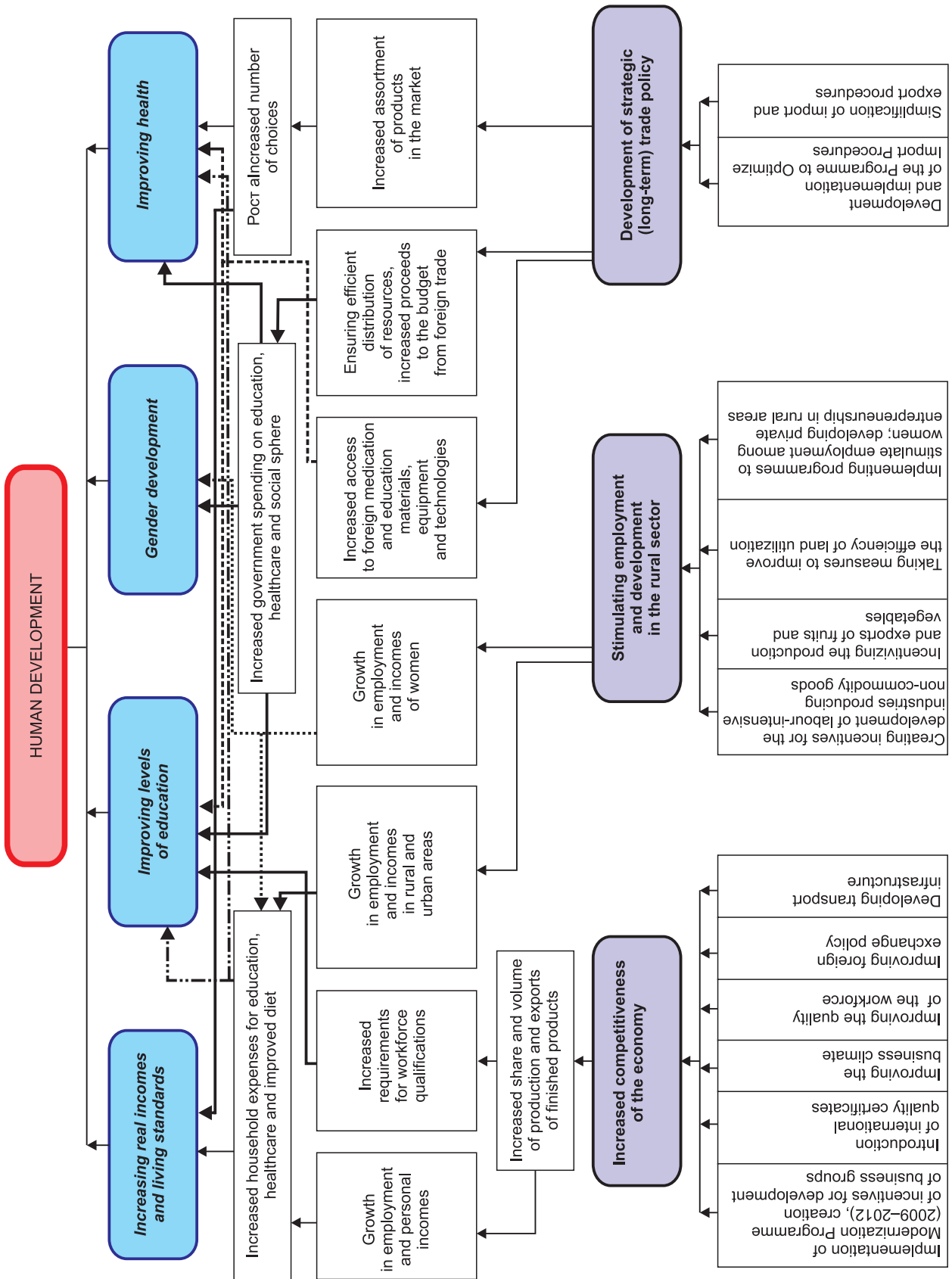
Equip national motor carriers with new automobiles, primarily Urta Osiyo Trans SJSC IRC and Hanjin Group JV, with a view to increasing the share of export-import shipments by national motor carriers to 50 percent.

3. Further optimization of transportation charges in the value of export cargoes of Uzbekistan, by:

- Establishing new optimized railroad tariffs together with countries participating in international transport corridors and a flexible system of tariff preferences, primarily to transit mineral fertilizers, cement, copper, cotton fibre, yarn and other export items, in 2010;
- Consider the gradual convergence of railroad tariffs to transport export cargoes with tariffs to transport domestic cargoes;
- Developing fares for transit shipments following the Farap-Turkmenbashi-Baku-Akhalkalaki-Kars route with further access to Central and Southern Europe.

The implementation of the above measures, aiming to develop transport and transit, along with a series of measures in other economic sectors, will provide an opportunity to increase the efficiency and utilize the potential of the trade policy in achieving high human development results in the long-term.

The main recommendations for which implementation would facilitate a more complete utilization of the trade policy's potential as one of the factors in human development, are presented below:



Conclusion

International experience illustrates that a close connection exists between foreign trade and human development. In particular, an increase in foreign trade and improvement of its structure contribute to the growth in overall economic efficiency, employment and personal incomes; and provide opportunities for people to improve their qualifications, to apply their skills in the job market, and to choose from goods presented in the domestic market.

However, rapid foreign trade liberalization in a country with a relatively low level of economic development and a majority of producers that are uncompetitive in the global market, can cause significant structural and social repercussions in the short-term, and reverse the potentially positive long-term effect.

Therefore, any foreign trade reform should be preceded by institutional reforms, which encourage a reduction in internal barriers for economic development, which primarily restrict the opportunities for the private sector to realize the benefits that emerge with such liberalization. When choosing a specific mechanism for reforming foreign trade policy it is important to take into account whether such reform will enhance the quality of institutions, and whether it will help in implementing the overall development strategy, including the achievement of human development goals.

In Uzbekistan, foreign trade policy has undergone significant changes at each stage of economic reform since independence. However, the trade policy had never been seen as an independent factor, and was treated as an instrument to achieve the goals of the macroeconomic, industrial and social policies of the government.

At the first stage of reform (1991-1994), foreign trade policy mainly served as a means of social stability and saturation of the domestic market with consumer products, through liberalization of imports and restriction of exports. During the second stage (1995-2000), the policy was primarily used to ensure macroeconomic stability and to stimulate investment activities in the real sector of the economy. At this stage, a foreign exchange control method was used, which provided contradictory results and allowed for large-scale investments in a series of strategic industries of the economy. The liberalization of the foreign exchange market during the third stage of economic reforms (after 2001) became an important factor in achieving high growth rates in exports and economic growth in the country, as well as for improving a number of human development indices. One of the most important events of the third stage was the global financial and economic crisis of 2008-2009.

In order to maximize the potential of the trade policy with the purpose of achieving high human development results in the post-financial crisis context, it is recommended to conduct the following reforms:

- Enhancing the domestic production capacity of both the private and public sectors, and increasing the competitiveness of the economy;

- Improving the quality of the workforce and human development;
- Developing a strategy for trade policy, targeting the achievement of high economic growth and human development goals in the long-term;
- Implementing reforms aiming to increase employment and personal incomes by stimulating production and exports in labour-intensive industries, and developing the rural sector;
- Developing transportation and transit as one of the main factors of an efficient trade policy targeting sustainable development.

The implementation of the proposed priorities and measures will allow for both increasing the efficiency of Uzbekistan's economy as a whole, and for realizing the potential of the trade policy as a factor in achieving high human development results.

Appendix 1. Human Development Index Dynamics in Uzbekistan

	1995	2000	2001	2002	2003	2004	2005 ⁵⁹
Human Development Index	0,715	0.736	0.740	0.742	0.748	0.751	0,759
GDP Index	0,498	0.532	0.535	0.542	0.550	0.565	0,580
Real GDP per capita (PPP, US\$)	1973	2422,0	2460,0	2573,6	2704,9	2954,3	3227,2
Life Expectancy Index	0,735	0.763	0.772	0.770	0.777	0.770	0,780
Life Expectancy at Birth, years	69,1	70,8	71,3	71,2	71,6	71,2	71,8
Education Index	0,913	0.913	0.913	0.913	0.917	0.917	0,917
Adult Literacy Level, %	99,0	99,17	99,18	99,19	99,20	99,31	99,36
Time at School, years	11,4	11,4	11,5	11,6	11,6	11,7	11,7

Source: National Reports on Human Development – Uzbekistan.

Dynamics of Major Macroeconomic Indices (2001–2008)

Index	2001	2002	2003	2004	2005	2006	2007	2008
GDP Growth, %	4.2	4.0	4.2	7.7	7.0	7.5	9.5	9.0
Budget Deficit (Surplus), as % of GDP	-1.0	-0.8	-0.4	-0.4	0.1	0.5	1.1	1.5
Inflation (CPI),%	26.6	21.6	3.8	3.7	7.8	6.8	6.8	7.8
Growth in Industrial Output, %	7.6	8.5	6.2	9.4	7.3	10.8	12.1	12.7
Growth in Agricultural Output, %	4.2	6.1	5.9	10.1	5.4	6.2	6.1	4.5
Growth in Investments, %	4.0	3.6	4.8	7.3	5.7	9.3	25.8	28.3
Growth in Exports, %	-0.1	-8.5	24.65	30.28	11.45	18.14	40.7	27.8

Source: State Committee of the RoU on Statistics

⁵⁹ Data for the periods after 2005, available in presently published national human development reports for Uzbekistan, is not presented here.

Appendix 2. Key Indices of Foreign Trade for the Republic of Uzbekistan (1991-2008)

	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
Foreign Trade Turnover	2063,2	4456,4	4554,6	5299,4	6612,6	9311,3	8910,5	6816,9	6346,5	6212,1	6401,8	5700,4	6689,2	8669	9500,1	10785,7	15719,6	19077,0
Including																		
CIS countries	0,0	2623,9	2630,2	3062,4	2540,8	2568,3	2776,8	1832,6	1792,7	2297,8	2285,4	1823,6	2105,4	3002,6	3403,4	4656,3	7679,1	7214,5
Other countries	2063,2	1832,5	1924,4	2237,0	4071,8	6743,0	6133,7	4984,3	4553,8	3914,3	4116,4	3876,6	4583,8	5666,4	6096,7	6129,4	8040,5	11862,5
Share of:																		
CIS countries	0,0	58,9	57,7	57,8	38,4	27,6	31,2	26,9	28,2	37,0	35,8	32,0	31,5	34,6	35,8	43,1	48,8	37,8
Other countries	100,0	41,1	42,3	42,2	61,6	72,4	68,8	73,1	71,8	63,0	64,2	68,0	68,5	65,4	64,2	56,8	51,1	62,2
Exports	677,4	2336,8	2399,6	2689,9	3719,9	4590,2	4387,5	3528,2	3235,8	3264,7	3264,3	2988,4	3725,0	4853	5408,8	6389,8	8991,5	11572,9
Including																		
CIS countries	0,0	1446,9	1466,6	1660,3	1282,4	1050,6	1508,6	917,1	982,8	1172,2	1113,4	823,5	969,2	1528,4	1722,6	2685,5	4273,0	4010,8
Other countries	677,4	889,9	933,0	1029,6	2437,5	3539,6	2878,9	2611,1	2253,0	2092,5	2150,9	2164,9	2755,8	3324,6	3686,2	3704,3	4718,5	7562,1
Share of:																		
CIS countries	0,0	61,9	61,1	61,7	34,5	22,9	34,4	26,0	30,4	35,9	34,4	27,6	26,0	31,4	31,8	42	47,5	34,6
Other countries	100,0	38,1	38,9	38,3	65,5	77,1	65,6	74,0	69,6	64,1	65,6	72,4	74,0	68,5	68,1	57,97	52,4	65,3
Imports	1385,8	2119,6	2155,0	2609,5	2892,7	4721,1	4523,0	3288,7	3110,7	2947,4	3136,9	2712,0	2964,2	3816	4091,3	4395,9	6728,1	7504,1
Including																		
CIS countries	0,0	1177,0	1163,6	1402,1	1258,4	1517,7	1268,2	915,5	809,9	1125,6	1172,0	1000,3	1136,2	1474,2	1680,8	1970,8	3406,1	3203,7
Other countries	1385,8	942,6	991,4	1207,4	1634,3	3203,4	3254,8	2373,2	2300,8	1821,8	1964,9	1711,7	1828,0	2341,8	2410,5	2425,1	3322,0	4300,4
Share of:																		
CIS countries	0,0	55,5	54,0	53,7	43,5	32,1	28,0	27,8	26,0	38,2	37,4	36,9	40,0	38,6	41,1	44,8	50,6	42,7
Other countries	100,0	44,5	46,0	46,3	56,5	67,9	72,0	72,2	74,0	61,8	62,6	60,1	60,0	61,4	58,9	55,2	49,4	57,3
Balance	-708,4	217,2	244,6	80,4	827,2	-130,9	-135,5	239,5	125,1	317,3	127,4	276,4	760,8	1037	1317,5	1988,2	2263,4	4068,8
With CIS countries	0,0	269,9	303,0	258,2	24,0	-467,1	240,4	1,6	172,9	46,6	-58,6	-176,8	-167,0	54,2	41,8	713,9	866,9	807,1
With other countries	-708,4	-52,7	-58,4	-177,8	803,2	336,2	-375,9	237,9	-47,8	270,7	186,0	453,2	927,8	982,8	1275,7	1274,4	1396,5	3261,7

Appendix 3. Commodity Structure of Exports and Imports of the Republic of Uzbekistan (1992-2008)

Structure of Exports of the Republic of Uzbekistan (1992-2000), %

	1992	1993	1994	1995	1996	1997	1998	1999	2000
Exports	100	100	100	100	100	100	100	100	100
Cotton Fiber	47,9	50	56,4	48,4	38,1	36	38,6	27,3	27,5
Chemicals and Plastics	4	4,7	3	2,5	2,4	1,7	1,5	3,1	2,9
Ferrous and Nonferrous Metals	9,4	6	4	4,7	3,5	4,6	5,1	4,3	6,6
Machinery and Equipment	9,4	9,1	8,1	2	2,8	6,3	4,1	3,2	3,4
Foodstuffs	3,2	2,9	4,1	4,7	4,5	3,8	3,2	6,4	5,4
Energy Products	14,8	19,5	14,2	11,7	6	12	7,9	11,5	10,3
Services	0	1,9	5,2	7,7	8,3	8,2	8,8	9,5	13,7
Other	11,3	5,9	5	18,3	34,4	27,4	30,8	34,7	30,2

Structure of Exports of the Republic of Uzbekistan (2001-2008), %

	2001	2002	2003	2004	2005	2006	2007	2008
Exports	100	100	100	100	100	100	100	100
Cotton Fiber	22	22,4	19,8	18,1	19,1	17,2	12,5	9,2
Chemicals and Plastics	2,7	3	3,1	4,7	5,3	5,6	6,8	5,6
Ferrous and Nonferrous Metals	7	6,4	6,4	8,6	9,2	12,9	11,5	7,0
Machinery and Equipment	3,9	3,9	5,9	7,4	8,4	10,1	10,4	7,5
Foodstuffs	3,9	3,5	2,7	3,8	3,8	7,9	8,5	4,4
Energy Products	10,2	8,1	9,8	12,4	11,5	13,1	20,2	25,2
Services	14,6	15,9	14,4	11,8	12,2	12,1	10,7	10,4
Other	35,7	36,8	36,9	33,2	30,5	21,1	19,4	30,7

Structure of Imports of the Republic of Uzbekistan (1992-2000), %

	1992	1993	1994	1995	1996	1997	1998	1999	2000
Imports	100	100	100	100	100	100	100	100	100
Energy Products	25,5	28	13,5	1,9	1,1	0,6	0,5	2,1	3,8
Ferrous and Nonferrous Metals	8,1	9,9	8,5	5,7	6,7	7,5	9,2	7,9	8,6
Foodstuffs	36,8	34,2	31,5	17,7	29,4	19,3	15,6	13,1	12,3
Machinery and Equipment	9,2	10,4	16,2	57,3	35,8	45,9	47,2	44,8	35,4
Chemicals and Plastics	7,5	8,2	7,6	9,4	12,5	12,5	12,4	11,7	13
Other	12,9	9	22	14,0	14,3	6,7	10,1	11,7	17,8
Services	0	0,3	0,3	5	0,2	7,5	5	8,7	8,5

Structure of Imports of the Republic of Uzbekistan (2001-2008), %

	2001	2002	2003	2004	2005	2006	2007	2008
Imports	100	100	100	100	100	100	100	100
Energy Products	1,9	1,3	2,7	2,1	2,5	4,3	3,5	2,1
Ferrous and Nonferrous Metals	10,9	8	7,9	10,3	10,3	10,4	7,5	6,8
Foodstuffs	10,8	12,5	9,9	6,8	7	8,1	7,2	8,1
Machinery and Equipment	41,2	41,4	44,4	46	43,3	40,3	49,6	53,3
Chemicals and Plastics	10,6	15,1	12,8	12,5	13,6	15	13,1	13,0
Other	14,3	11,1	12,0	11,2	12,9	12,8	13,3	11,0
Services	10,3	10,6	10,2	11,1	10,4	9,1	5,8	5,7

Appendix 4. Procedure for Executing a Standard Export Contract (non-standard procedures are highlighted)

No	Procedure	Submitted Documents
1	Contract registration with an authorized bank	Application Original contract and a copy Other documents (if the export operation is not standard)
2	Contract registration with Currency Control Department under the State Customs Committee or with local customs authorities	Application Original contract and a copy, stamped by the bank Other documents (if the export operation is not standard)
3	Executing an agreement with a shipping company to obtain car initials	Letter requesting to issue car initials Copy of the contract
4	Obtaining car plan from Uzbekistan Temir Yullari SJSRC	Copy of the contract Certificate on issued car initials Paid invoice, confirming payment for r/r shipment
5	Obtaining certificates of origin from Uzbekexpertiza OJSC	Application for certificate Copy of the contract Paid invoice, confirming payment for certificate Other documents (information on the producer, raw materials and components used in the production)
6	Executing an agreement with a broker and filling of CCD	Letter requesting to enter into an agreement Original contract and a copy Transportation and shipping documents (container and car numbers, railroad waybill) Summary of calculations (only for hard currency exports) Certificates (of origin, conformity and others, in cases stipulated by the legislation)
7	Registration of CCD and goods with customs authorities	CCD Original contract and a copy Transportation and shipping documents (container and car numbers, railroad waybill) Summary of calculations (only for hard currency exports) Certificates (of origin, conformity and others, in cases stipulated by the legislation)
8	Customs inspection, sealing and shipping	
9	Contract deregistration with an authorized bank	Application for contract deregistration Certificate of contract registration with customs authorities Confirmation of complete payment under the contract Shipping documents
10	Contract deregistration with Currency Control Department under the SCC or with local customs authorities	Application for contract deregistration Original contract and a copy Bank confirmation of complete payment under the contract
11	Obtaining certificates of conformity from Uzstandard Agency	Application for inspection and certificate Original contract and a copy Hygiene certificate Phytosanitary or veterinary health certificate Confirmation of payment for certification services
12	Obtaining phytosanitary, hygiene certificates	Application for inspection and certificate
13	Export contract registration with MFERIT	Application for contract registration Original contract and a copy Copy of export license (for specific contracts) Permissions of authorized state bodies to export (in cases stipulated by the legislation) Legal opinion on the contract (regarding its conformance with the legislation, in case if the contract amount exceeds 200 minimum wages, issued in a manner, established by the legislation) Competitive list or justification of contract price (with supporting documents)
14	Obtaining MFERIT license to export specific items	Application for export license Resolution of the Cabinet of Ministers of RoU permitting exports Original contract and a copy Certificate of origin
15	Obtaining Cabinet of Ministers' permission to export used equipment	Application for inspection of used equipment Original contract and a copy Certificate of origin

Appendix 5. Procedure for Executing a Standard Import Contract (non-standard procedures are highlighted)

1	Contract registration with an authorized bank	Application Original contract and a copy Passport of import transaction Other documents (if the export operation is not standard)
2	Contract registration with Currency Control Department under the SCC or with local customs authorities	Application Original contract and a copy, stamped by the bank Passport of import transaction Other documents (if the export operation is not standard)
3	Conversion of funds	Application Copy of the contract with customs stamp
4	Application to Uzbekistan Temir Yullari SJSRC to receive the shipment	Copy of the contract Paid invoice, confirming payment for r/r shipment
5	Executing an agreement with a broker and filling of CCD	Letter requesting to enter into an agreement Original contract and a copy Transportation and shipping documents (container and car numbers, railroad waybill) Copy of invoice Certificates (of origin, conformity and others, in cases stipulated by the legislation)
6	Registration of CCD and goods with customs authorities	CCD Original contract and a copy Transportation and shipping documents (container and car numbers, railroad waybill) Invoice Certificates (of origin, conformity and others, in cases stipulated by the legislation)
7	Customs inspection, sealing and shipping	
8	Contract deregistration with an authorized bank	Application for contract deregistration Original contract and a copy Copy of CCD
9	Contract deregistration with Currency Control Department under the SCC or with local customs authorities	Application for contract deregistration Original contract and a copy Copy of passport of import transaction Bank confirmation of complete payment under the contract
10	Obtaining certificates of conformity from Uzstandard Agency	Application for inspection and certificate Original contract and a copy Hygiene certificate Phytosanitary or veterinary health certificate Confirmation of payment for certification services
11	Marking of imported goods	
12	Obtaining phytosanitary, hygiene certificates	Application for inspection and certificate Original contract and a copy Confirmation of payment for certification services
13	Import contract inspection by MFERIT	Application for contract inspection Original contract and a copy Copy of import license (for specific contracts) Permissions of authorized state bodies to import (in cases stipulated by the legislation) Legal opinion on the contract (regarding its conformance with the legislation, in case if the contract amount exceeds 200 minimum wages, issued in a manner, established by the legislation) Competitive list or justification of contract price (with supporting documents)

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ACTION MATRIX IMPROVING TRADE POLICY WITH A VIEW TO FURTHER HUMAN DEVELOPMENT							
No.	Goal	Recommended Action	Measures	Indicators	Timeframe	Agencies, responsible for implementation	Donors
Key goal: improving living standards and quality of life, improving educational and health indicators, reaching gender equality							
1.	Growth of productive employment and personal incomes, subsequent increase in household spending on education, healthcare, improved diet and living standards; achieving gender equality; human development.	1.1. Take measures to improve the competitiveness of the economy	1.1.1. Implementation of Industry Modernization Program (2009-2012); creating stimuli for developing business groups	The share of finished products in exports increased by 10-20%; Achieved annual real cash income growth rate of 30-40%	2010-2015	Ministry of Economy, MFERIT, URDF, Ministry of Finance, major business associations and enterprises	UNDP, USAID, WB, ADB
			1.1.2. Introduction of international quality standards (ISO) for a wide range of products manufactured in the republic and that are exported			MFERIT, SCC	
			1.1.3. Improving the business climate and eliminating domestic barriers for productive entrepreneurial activities			SCC, MFERIT, CCI	
			1.1.4. Setting and maintaining a real exchange rate at a level ensuring the competitiveness of exports			CB	
			1.1.5. Developing transport infrastructure and transit				
1.	1.2. Take measures to improve the quality of the workforce and human development	1.2.1. Improving educational system	1.2.2. Increasing the efficiency of health care system	The share of employed SVSE graduates according to their specializations increased by 30%	2010-2015	Ministry of Higher and Secondary Special Education	UNDP, USAID, UNICEF
				The number of employed graduates of higher educational institutions per 10 thousand people increased by 40%		Ministry of Health	
				The number of incidents of main group of diseases per 100 thousand people reduced by 10-20%. The mortality rate per 100 thousand people reduced by 15-20%			

ACTION MATRIX IMPROVING TRADE POLICY WITH A VIEW TO FURTHER HUMAN DEVELOPMENT							
No.	Goal	Recommended Action	Measures	Indicators	Timeframe	Agencies, responsible for implementation	Donors
Key goal: improving living standards and quality of life, improving educational and health indicators, reaching gender equality							
1.	Growth of productive employment and personal incomes, subsequent increase in household spending on education, healthcare, improved diet and living standards; achieving gender equality; human development.	1.3. Incentivize employment and development of agricultural sector	1.2.3. Taking measures to enhance social infrastructure	Percentage of population with access to central water supply and natural gas increased by 10%	2010-2015	Ministry of Economy CCI, MFERIT Ministry of Agriculture and Water Management Women's Committee, Business Women's Association, Mehr Association of Women's NGO	UNDP, USAID, UNICEF
			1.3.1. Creating stimuli for the development of labour-intensive industries producing non-commodity items with high value addition 1.3.2. Incentivizing production and exports of fruits and vegetables 1.3.3. Increasing the efficiency of land resource utilization 1.3.4. Implementing programs to increase employment among women, developing private entrepreneurship in rural areas	The negative impact of farm-consolidating reforms on employment is leveled out Annual employment growth rate of 3-3.5% achieved Equal shares of females and males in total employed population achieved	2010-2015		
2.	Provide for efficient distribution of resources and increased government spending in the different social spheres and for human development		2.1.1. Developing and implementing an import regime optimization programme 2.1.2. Simplifying import and export procedures: - Implementing the program of introducing 'One Window' mechanism, allowing for one channel for completing all customs formalities; - Implementing a program of automation of customs administration and control; introduction of preliminary and electronic declaration, introduction of a system for post-customs control	Budget revenues from foreign trade operations increased by 15-20%; Time for completing export and import procedures reduced by 30%	2010-2014	MFERIT, SCC MFERIT, SCC	UNDP, USAID, WB, ADB, IFC



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