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Online Consultation for the Preparation of the Uzbekistan Systematic Country Diagnostic

Input to the Country Partnership Framework 2015-2019

August 2015

Presentation Outline

1. Preamble
2. Salient features of Uzbekistan's development
3. The sustainability challenge
4. Selected policy questions (for discussion)
5. Next steps

Preamble

- The *Systematic Country Diagnostic* (SCD)
 - Designed to be the main analytical input into the [Country Partnership Framework](#) (CPF), which outlines the World Bank Group's (WBG) medium term engagement strategy in a country
 - Is an analysis produced by WBG teams, benefitting from consultation with government and stakeholders
 - Lays out country opportunities and challenges to:
 - Eradicating extreme poverty AND/OR
 - Boosting “shared prosperity” by promoting income growth for those at the bottom 40% of the income distribution.
- Each SCD is [adjusted to country circumstances](#)
- Main analytical questions for Uzbekistan's SCD include:
 - What are challenges to maintaining high GDP growth?
 - What are challenges to creating more jobs?
 - What are challenges to creating more good jobs?
 - What are challenges to improving economic well-being?
 - What are challenges to sustaining economic, environmental and social outcomes?

Preamble

Purpose of consultation:

To solicit feedback on the initial findings and analytical questions of the SCD, and in particular:

- The validity / accuracy of the emerging conclusions;
- Any additional considerations, whose omission would affect the likelihood / pace of progress on poverty reduction or increases in shared prosperity

Some specific questions readers may wish to comment on can be found on slides **20, 28, and 30-34**. Comments on other parts of the presentation are of course welcome.

Presentation Outline

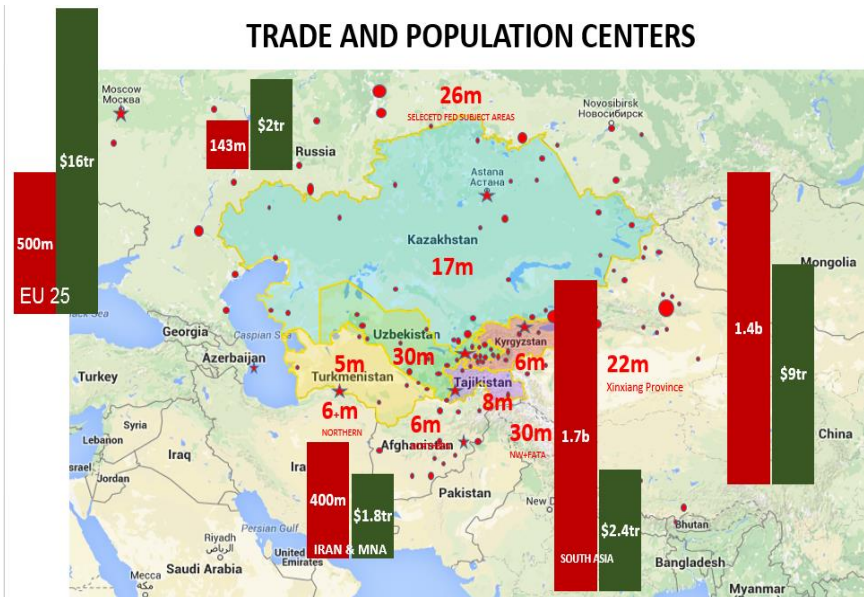
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Salient features: endowments

Uzbekistan has much going for it!

A central/strategic position in the region and large domestic market

A young, growing, relatively well-educated population

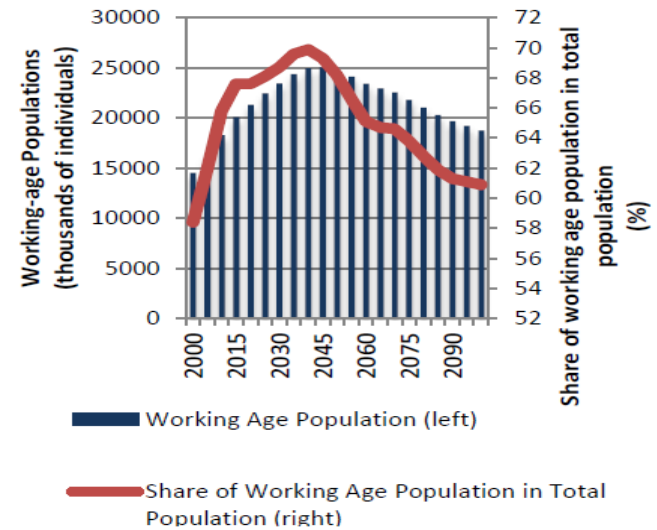


For Central Asia, country populations are in millions. For adjacent countries, populations figures refer only to populations of regions or districts adjacent to Central Asia.

Sources: WB World Development Indicators

- In addition **Uzbekistan has significant mineral wealth** -Natural resources rents are estimated to be 20% of GDP (Source: World Bank – World Development Indicators)
- But there are also challenges:
 - While Uzbekistan borders all other countries in CA, it is ‘double-landlocked’
 - Uzbekistan is highly dependent on water originating in neighboring countries

Working Age Population in Uzbekistan

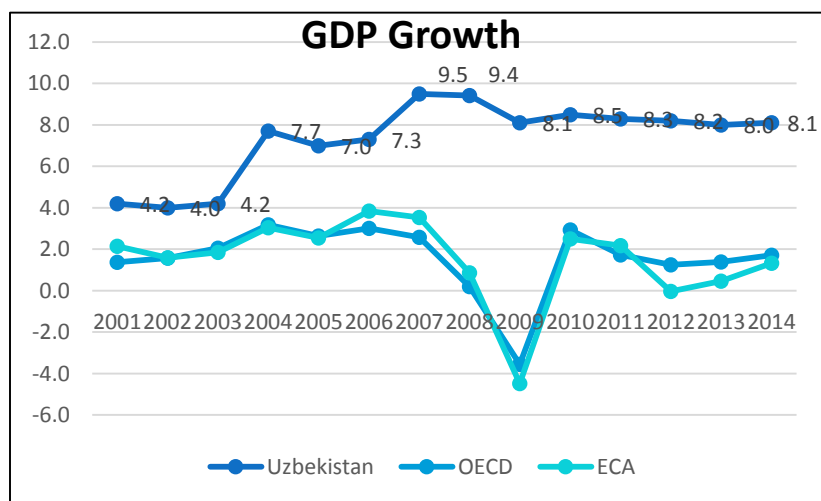


Source: WB calculations using UN, World Population Prospects, 2012

Salient features: economic performance

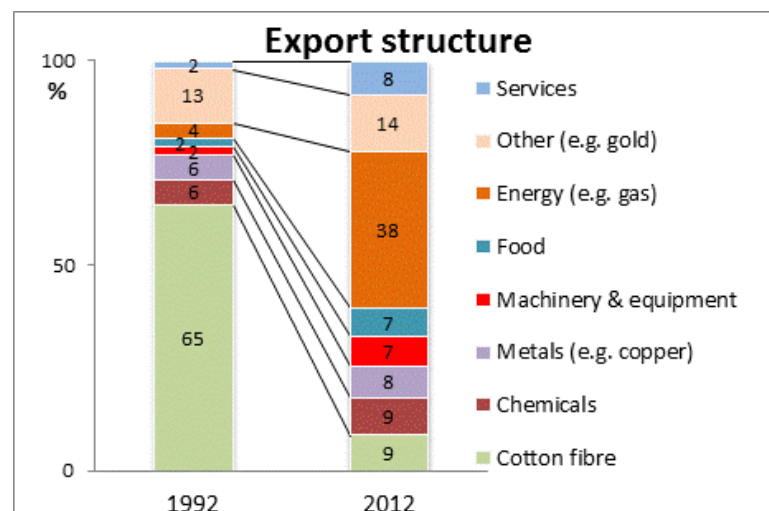
Overall, Uzbekistan has done extremely well over the past decade

It has achieved high and sustained growth



Source: Uzbekistan Ministry of National Economy / WDI

With some economic diversification



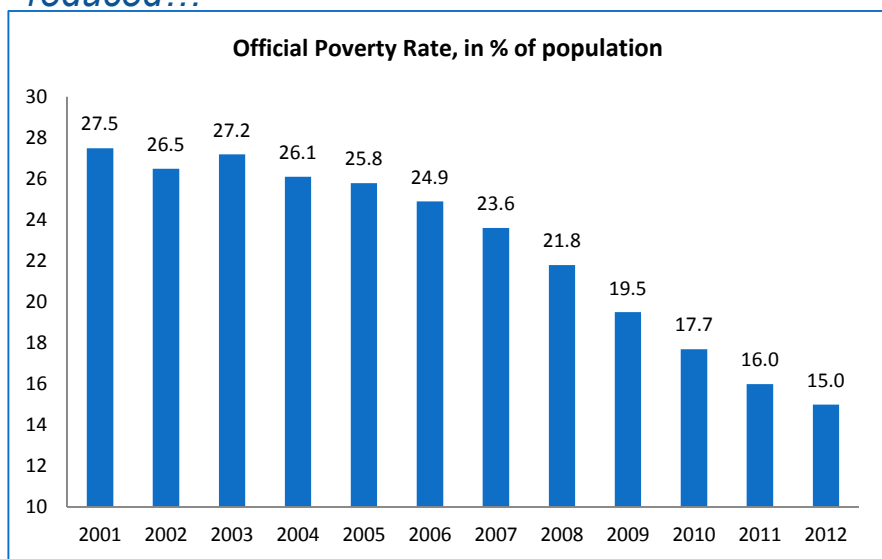
Source: UN COMTRADE, mirror statistics

POLICY QUESTION: Can the current GDP growth rates be sustained as: (1) external environment has changed, (2) diversification has come in low-tech products with limited integration in global value chains, and sustainability is questionable.

Salient features: relative poverty

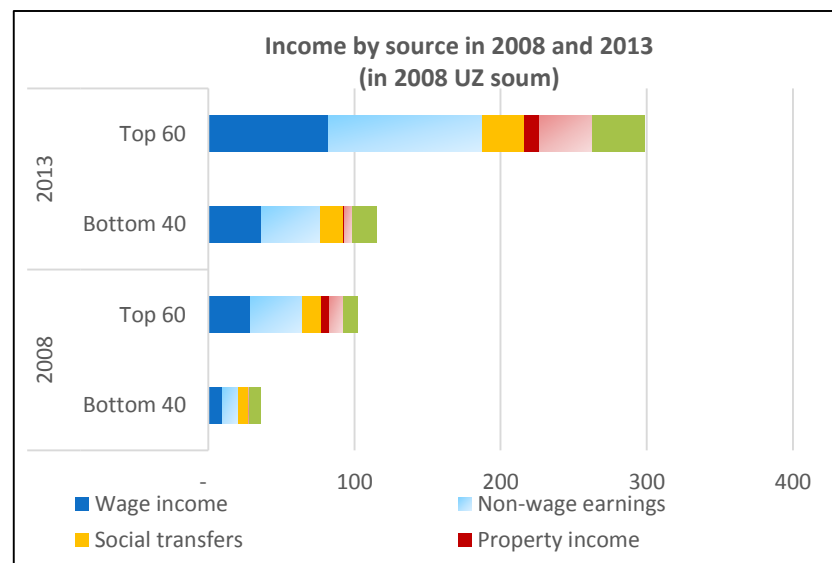
High growth has translated into improved welfare outcomes

According to official estimates, poverty has been reduced...



Source: Government estimates, GOU

...and shared prosperity has been maintained



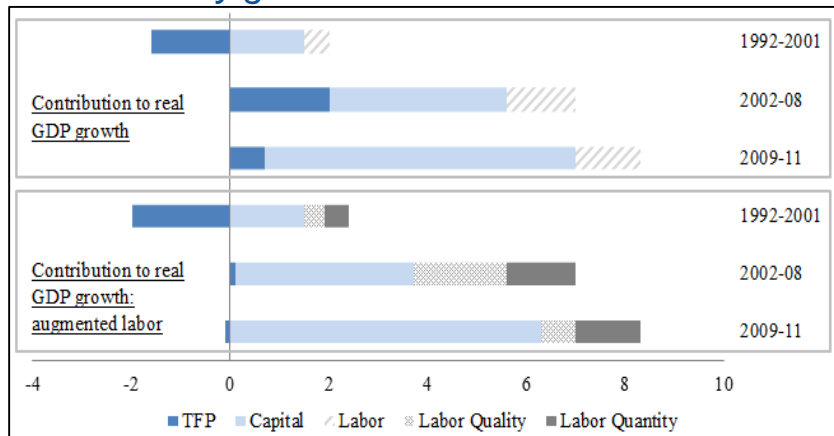
Note: Real monthly income per capita in 2008 constant UZ soum
Source: Household Budget Survey, Government of Uzbekistan

- **ANALYTICAL QUESTION:** While national accounts statistics and poverty statistics are not verifiable and subject to methodological uncertainty, one analytical question is if poverty reduction could have been faster given (i) high economic growth and (ii) relative initial equality.

Salient features: growth drivers

Growth has been driven by capital accumulation, likely coming from the state sectors

Labor growth and productivity gains are underutilized with low Total Factor Productivity growth



Source: IMF Article IV, 2012 Source: Government of Uzbekistan, National Statistics

The public sector remains very active in economic activity

- WB estimates that the public sector is at least 40 percent of GDP and 33 percent of employment
- Private sector firms tend to be small, informal and inward looking
- FDI remains limited relative to the size of the economy

Source: Government of Uzbekistan, National Statistics and World Bank

POLICY CHALLENGE: Over the medium run, Uzbekistan will need to identify and prioritize reforms to gradually increase the private sector's role in:

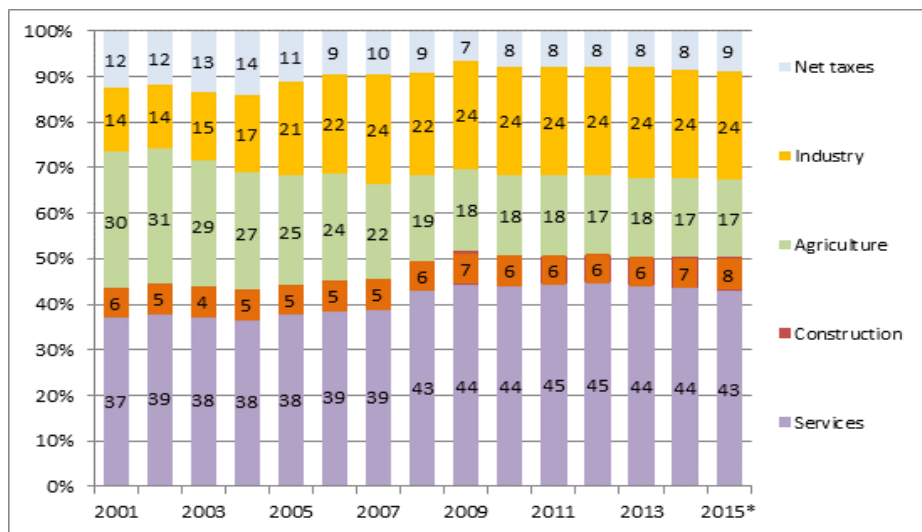
- **Total Factor Productivity (TFP) growth**
- **Employment creation**

Salient features: changes in employment

Uzbekistan's employment shares have changed as the structure of the economy has changed

Increases in both services and industry shares had made up for a significant drop in agriculture share in GDP

However the share of employment in industry has not increased underscoring that industrial sectors in Uzbekistan are relatively capital intensive



Source: Government of Uzbekistan, National Statistics and World Bank calculations



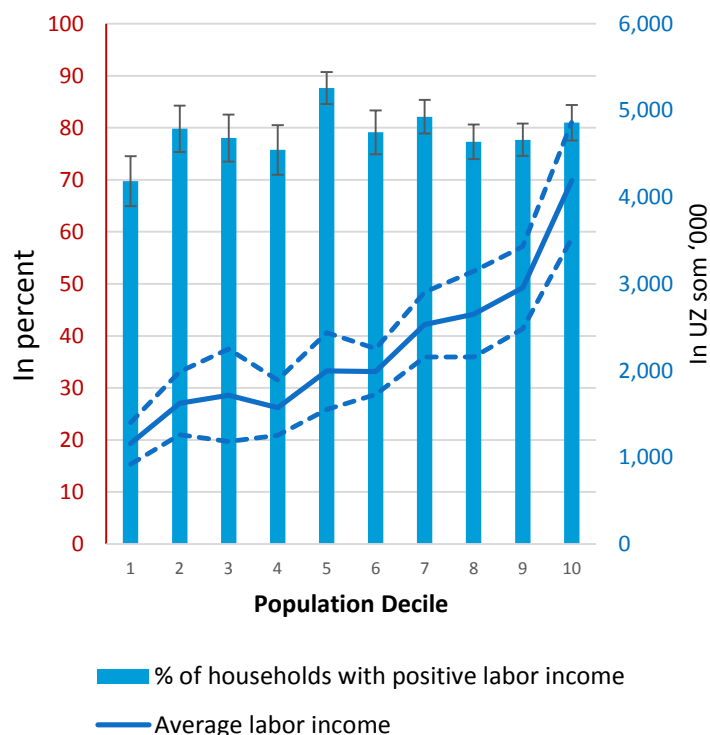
Source: Government of Uzbekistan, National Statistics and World Bank calculations

POLICY QUESTION: Would be sensible from an economic and social perspective for Uzbekistan to be investing in more labor intensive industries?

Salient features: income

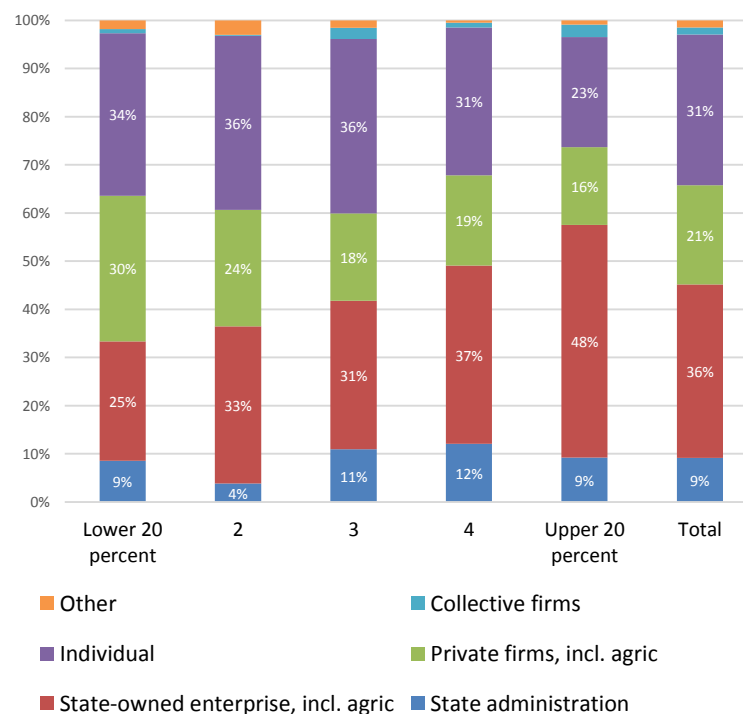
Differences in household welfare derive essentially from variations in labor income and type of employer

Labor compensation is the main source of income in all groups but with sharp variations in remuneration



Source: WB Calculations using CALISS

With significantly higher incomes derived from SOE employment



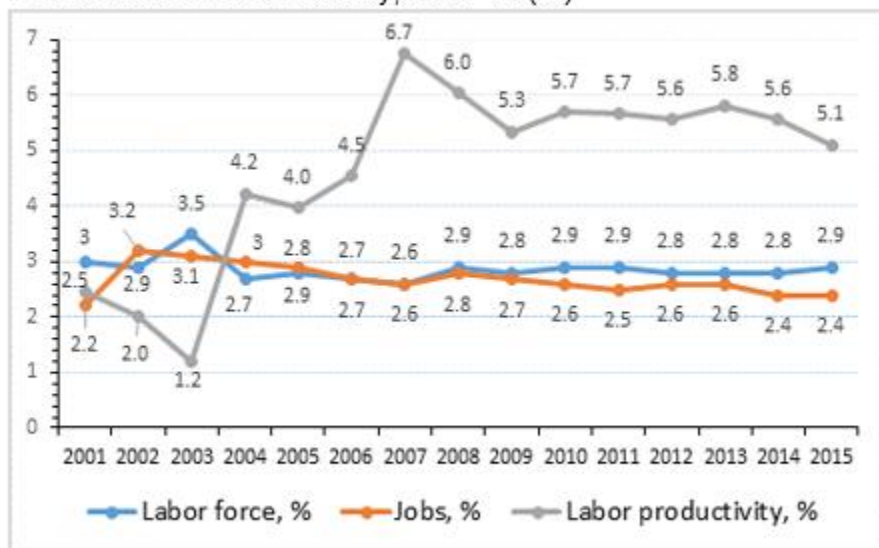
Source: WB Calculations using CALISS

Salient features: jobs

Jobs are not created fast enough and many are not high quality jobs

Labor force growth is outpacing job creation...

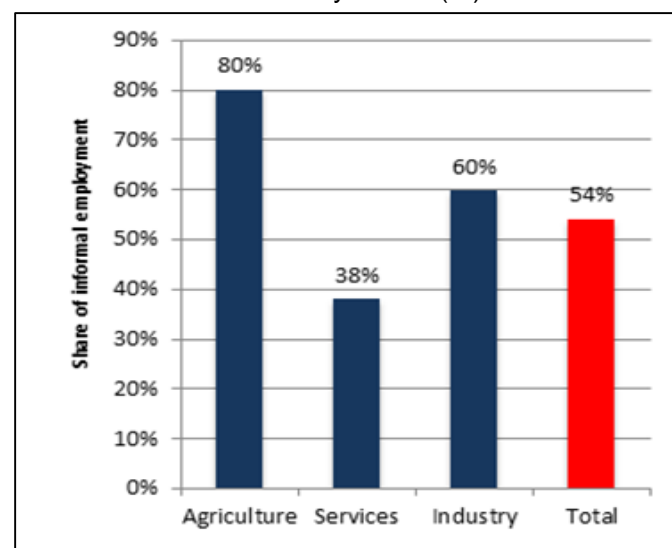
Labor Force and Productivity, 2001-15 (%)



Source: Uzbek authorities

... with widespread informality in the economy

Informal salaried work by sector (%)



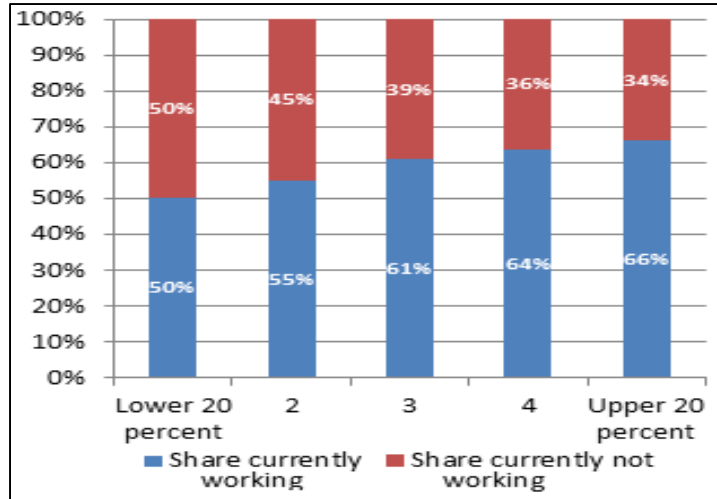
Source: WB calculations using World Bank/GIZ, Uzbekistan Jobs, Skills, and Migration Survey, 2013.

ADDITIONAL EVIDENCE: Officially, in 2012–13 unemployment was 4.9 percent of the working age population and in 2014 it was 5.1 percent, not counting labor migrants abroad. According to Russia's Federal Migration Service, Russia's economic slowdown in 2014 caused about 200,000 Uzbek migrants to return home. The number of registered Uzbek workers in Russia declined by 7.3 percent in 2014, from 2.5 million in December 2013 to 2.3 million in December 2014.

Salient features: jobs (cont.)

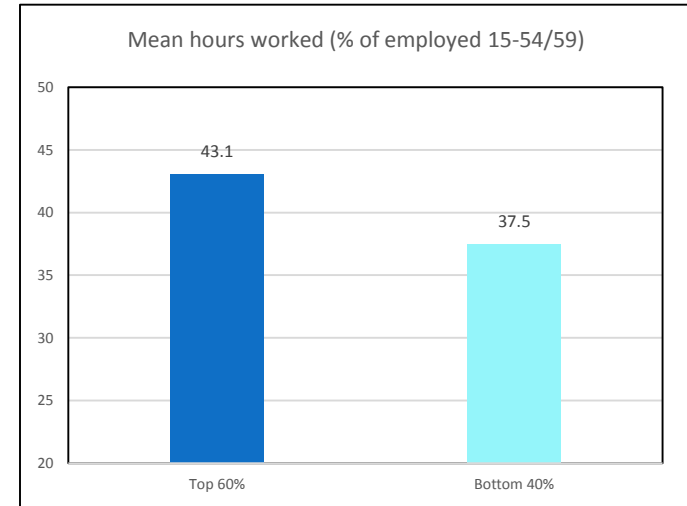
Although unemployment is low, many at the bottom of the income distribution opt out of the labor market, and work less

Labor force participation drops at the bottom of the distribution



Source: WB Calculations using CALISS

...as well as labor supply



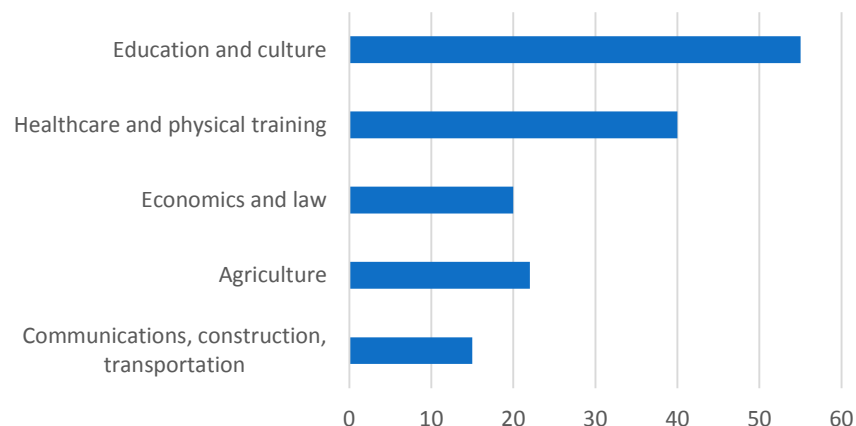
Source: WB Calculations using CALISS

Salient features: gender

There are distinct gender patterns in labor market access and participation

Women make up only 36% of students in tertiary education, and choose traditional “female” fields of study:

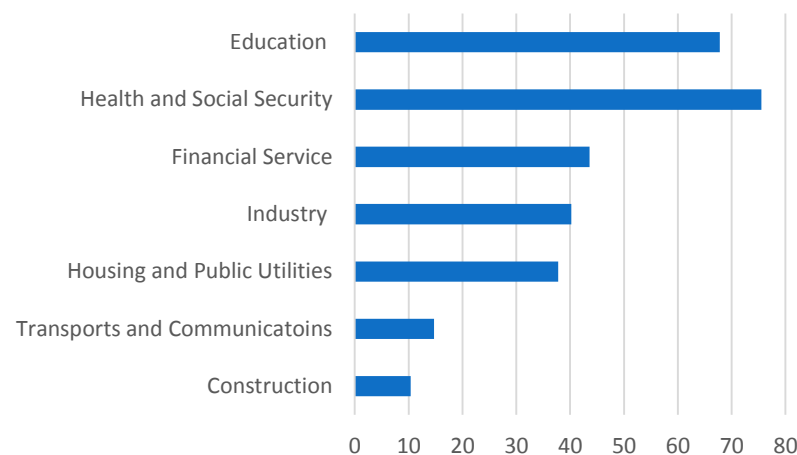
Share of Women in Tertiary Education by area



Source: State Committee of the Republic of Uzbekistan on Statistics (2014) Annual Statistical Compendium, Tashkent

Share of women among officially employed is only 40%, and they are concentrated in public service, which is lower paid:

Share of Female Labour Force by Sector

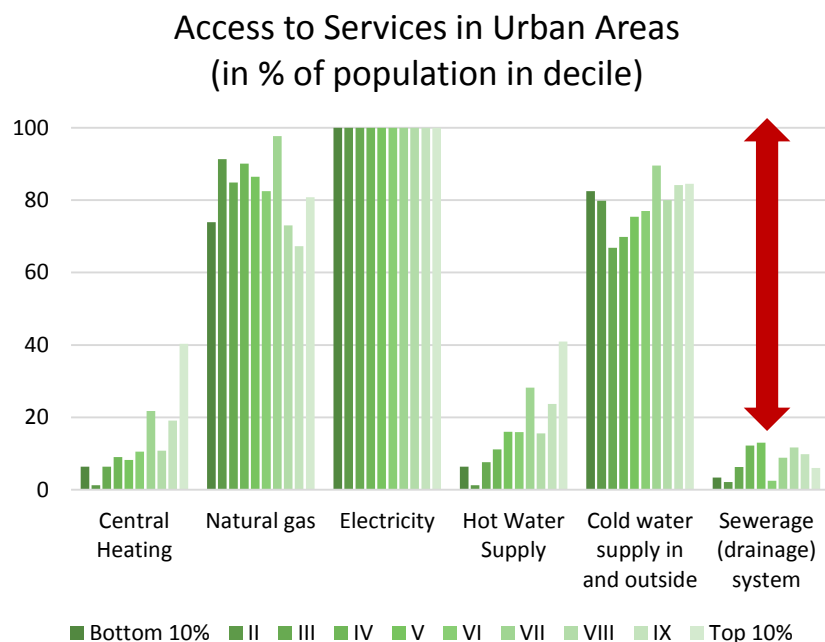


Source: ADB (2014) Uzbekistan Country Gender Assessment, Gender and Development, Central and West Asia, Asian Development Bank

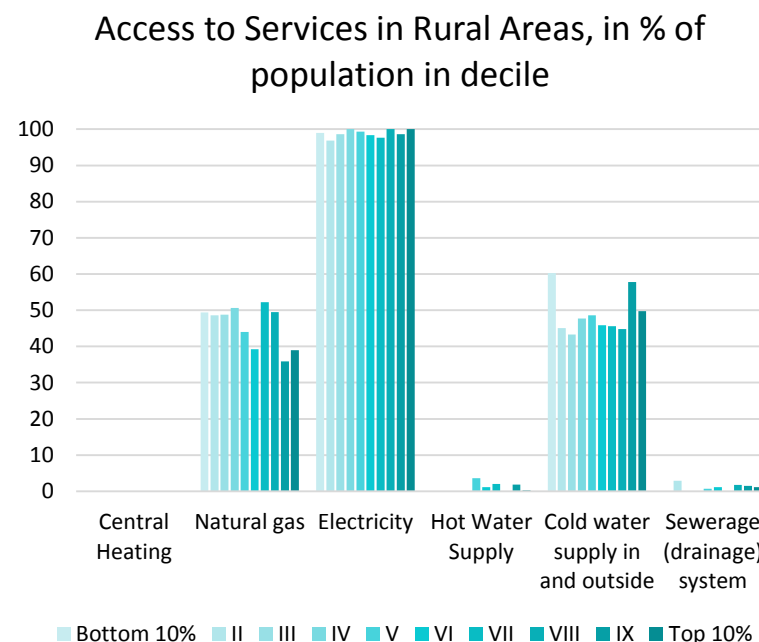
OBSERVATION: Life expectancy is higher for women than men – 75 vs. 71, while retirement age is lower - 55 vs. 60; thus the likelihood of old age poverty for women is higher. In agriculture, women comprise over 53%, but only 5.5% of farms are headed by women.

Salient features: communal infrastructure

Some gaps in the provision of communal infrastructures services, but more gaps for rural than for urban residents



Source: HBS, GOU (2013)



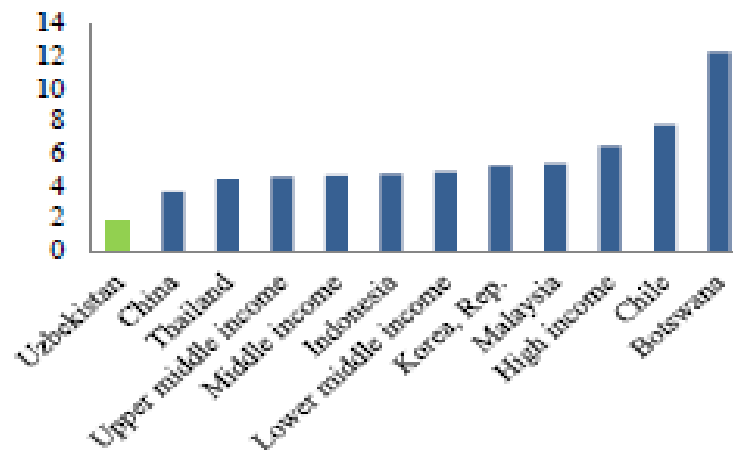
Source: HBS, GOU (2013)

- OBSERVATIONS:**
- (1) Higher income doesn't ensure access to basic infrastructure services
 - (2) Rural access to water and sewerage systems are much lower than in urban areas
 - (3) Also, access does not ensure regular availability of supply nor quality of services
 - (4) Water losses are estimated at 42%, and only about 33% of user connections are metered

Salient features: energy efficiency

Uzbekistan has low energy efficiency owing to demand and supply side inefficiencies and lack of investment. Current policies are likely to result in energy shortages in the future

Efficiency of electricity usage remains low as measured by GDP per unit of energy



GDP per unit of energy use (constant 2005 PPP \$ per kg of oil equivalent)

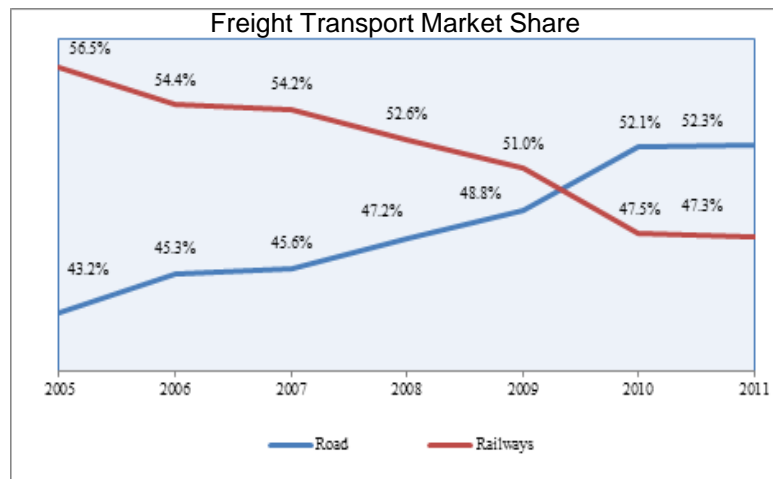
Source: World Development Indicators, 2012 World Bank.

EVIDENCE: Uzbekistan lost US\$2 billion in 2011 or 4.5% of GDP due to energy inefficiency, while 40% of available generation capacity will reach the end of service life by 2017. Additionally, despite rising domestic prices, energy tariffs remain below long-run supply costs.

Salient features: transport and logistics

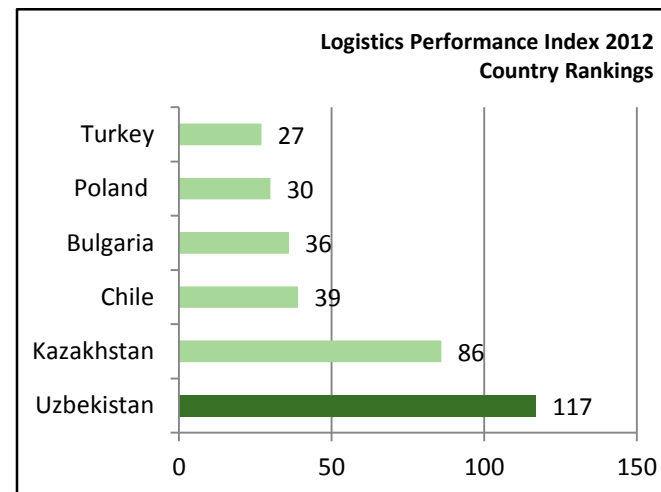
Transport: poor condition of roads and railways and a lack of logistics affects “connectivity”, trade flows and thus economic growth

Mode of transport has shifted from rail to roads creating significant rehabilitation backlogs



Source: Data reported by Uzbekistan Railway, 2012.

Rehabilitation backlogs lead to a significant trade barriers, with low logistics quality and a transport network that is not integrated

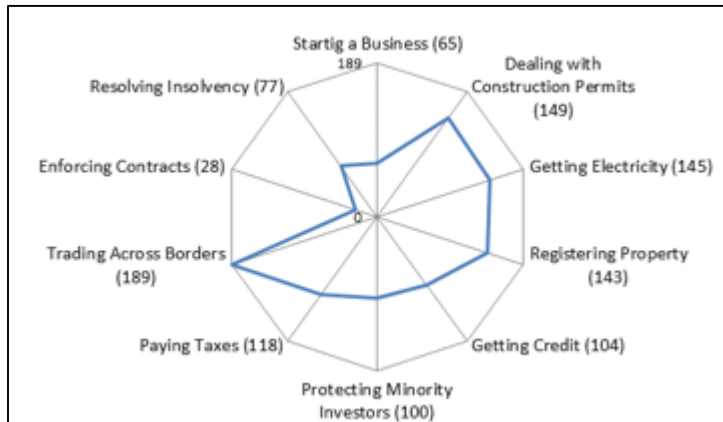


Source: World Bank, LPI 2012.

Salient features: business environment

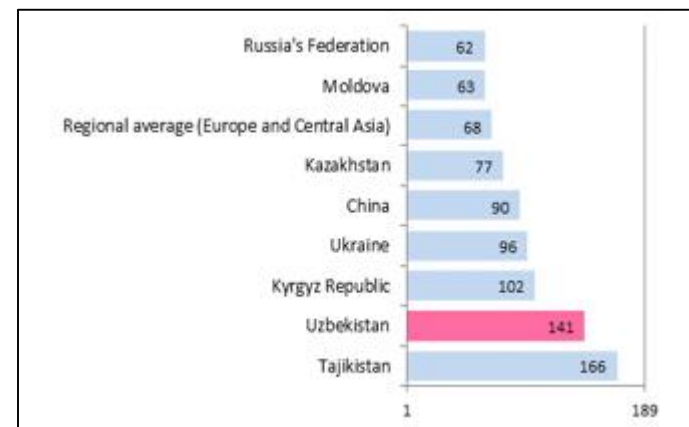
While business regulations have improved in recent years, Uzbekistan continues to lag in time and cost to comply with basic regulations

Uzbekistan has recently made progress in the DB ranking, but some of the DB indicators need to improve especially if Uzbekistan were to capitalize on geographic location



Source: WBG Doing Business Indicators 2015

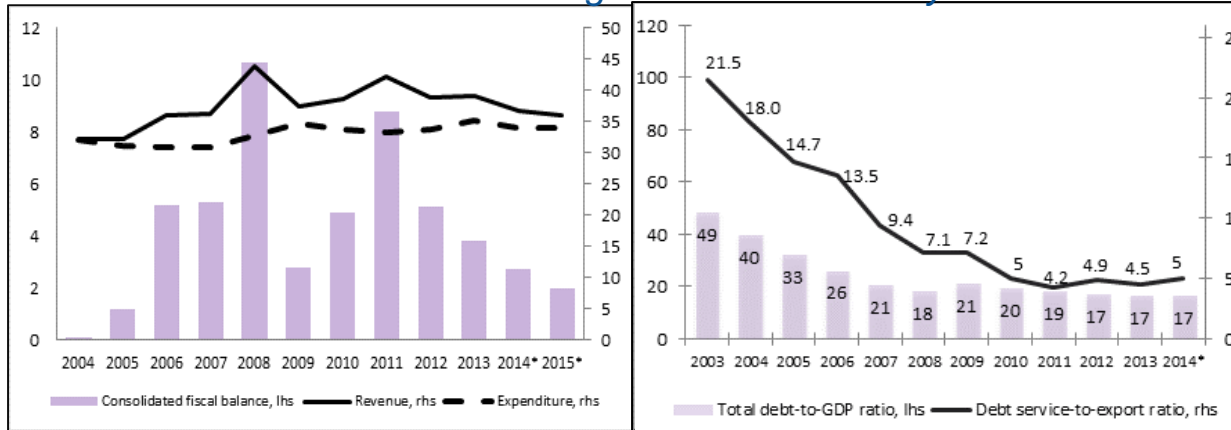
Compared to other countries Uzbekistan's poor overall DB ranking points to the difficulties that the private sector faces in operating



Source: WBG Doing Business Indicators 2015

Salient features: macroeconomic and financial policies

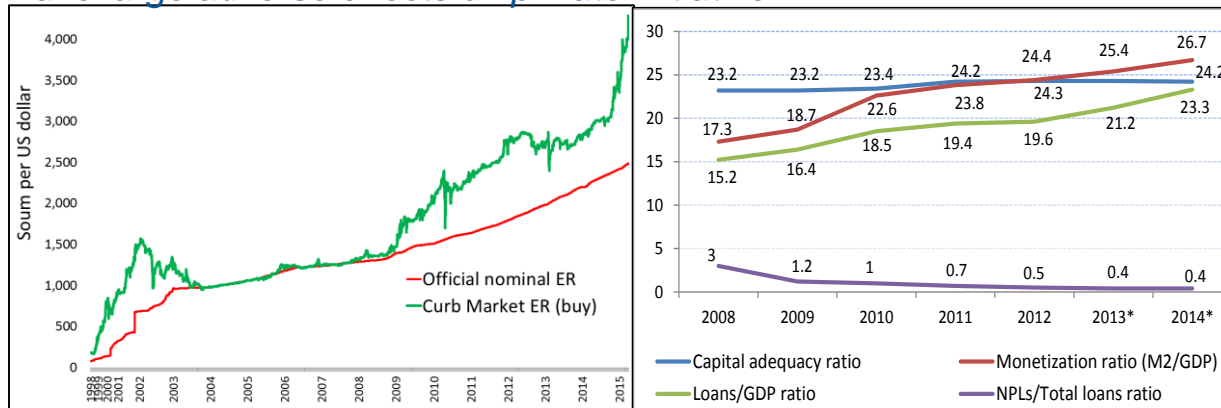
Prudent fiscal management has allowed debt levels to decrease and bodes well for the economic management of the country..



Source: Government of Uzbekistan

Source: Government of Uzbekistan

But a cumbersome exchange rate system and a small financial sector have large adverse effects on private initiative



Source: Government of Uzbekistan

Source: Government of Uzbekistan

Salient features of Uzbekistan's development

This section has shown

1. High economic growth
2. High savings and investment
3. Some economic diversification
4. Falling poverty

But concerns over:

1. The sustainability of the growth model
2. A deficit of good jobs created
3. Some inequities in access to jobs and services (across income and location)

This section raised some questions

1. With relatively high savings in Uzbekistan, why are not more jobs created?
2. What policies have prompted high capital intensity?
3. Is high capital intensity relatively more specific to some sectors or regions?
4. What is driving the rising wages?
5. Are wage increases relatively more specific to some sectors or regions?

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The sustainability challenge

Natural resources have played a key role in driving economic growth

However utilization and efficiency rates suggest that these trends are unsustainable

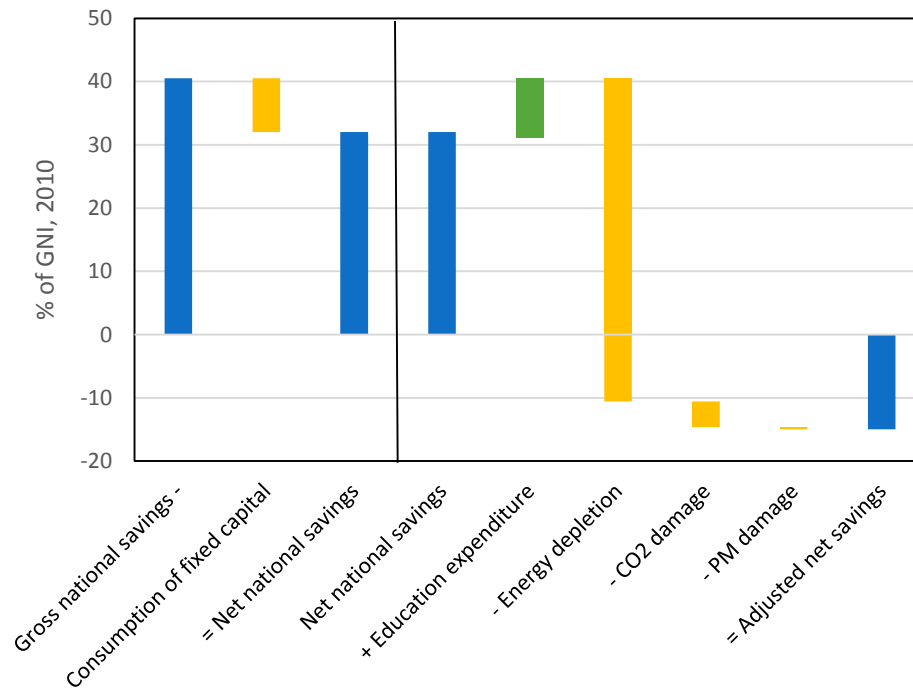
- Water intensity and efficiency in agriculture
- Energy intensity and efficiency on demand and supply sides

Ultimately those likely to be impacted the most are the poor: they are proportionately more dependent on natural resources for their livelihoods (e.g. agriculture).

The sustainability challenge: net wealth

Uzbekistan is losing wealth (future income) under its current growth model

Adjusted Net Savings (ANS) is negative - after accounting for natural resource degradation and depletion factors such as energy



Main drivers of natural resource dependence:

- Population growth, increasing affluence
- Finite natural resources under pressure
 - Water
 - Fossil and renewable energy
 - Land/ Forests
 - Biodiversity
- Climate change

Source: World Development Indicators, 2014, World Bank.

The sustainability challenge: water

Water: inefficient use is placing pressure on existing stocks that could be allocated to higher value production or consumption

- Only 10% of all land is arable and irrigating this land uses 90% of total water withdrawals
- Irrigation efficiencies in certain areas are as low as 30%
- Institutional issues: prices are not set at cost recovery levels, water infrastructure is degrading, and thus service delivery is poor
- A cubic meter of water used to irrigate grapes in Fergana generates 625 UZS, compared to 169 UZS for cotton; a cubic meter of water in Samarkand used to grow apples generates UZS 1,829, compared to 169 UZS for wheat

Water footprint and value generated for sample crops

	Price ('000 UZS) per ton	Water (m ³) footprint per ton	UZS per m ³ of water
Fergana grapes	1,500	2,400	625
Fergana cotton	750	4,426	169
Samarkand apples	1,500	820	1,829
Samarkand wheat	350	2,068	169

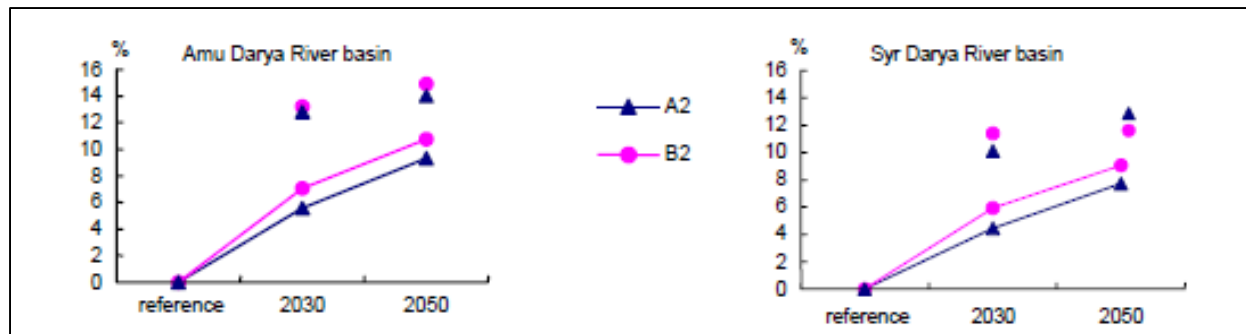
Source: Larson, D., D. Khidirov & I. Ramniceanu, 2015. "Uzbekistan: Strengthening the Horticulture Value Chain," World Bank Other Operational Studies 21495, World Bank.

The sustainability challenge: water (2)

In the longer-term, Syr Darya and Amu Darya river flows may decrease by 25-50% by 2050.

- More winter precipitation, higher variability as a result of climate change
- Irrigation rates will have to increase to compensate for this loss

Projected increase in mean and maximum irrigation rates to compensate for losses of agricultural crop yield associated with evaporation increases in the Amu Darya and Syr Darya river basins

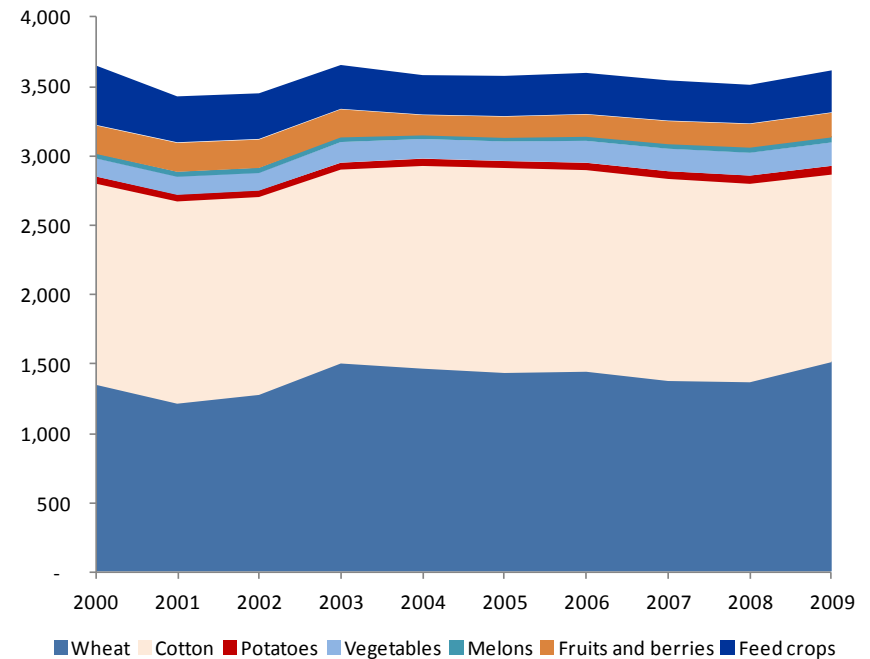


Source: Uzbekistan's Second National Communication, 2008.

The sustainability challenge: agriculture

Exceptional agro-climatic conditions and strong support for productive technologies are the foundation of a strong and growing agricultural sector in Uzbekistan, but farmers need greater flexibility in making full use of limited land and water

Land available for agriculture is limited as is the potential for increasing irrigated land

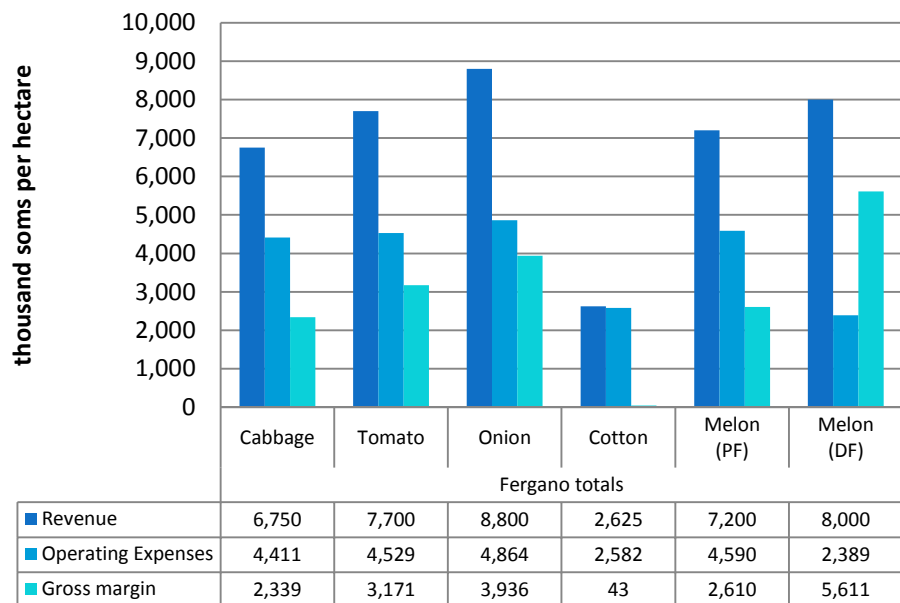


Source: State Committee on Statistics, Uzbekistan.

The sustainability challenge: agriculture (2)

Land leases requiring cotton and wheat production quotas keep much of the land locked in old production patterns, even though fruit and vegetable crops are more profitable in some areas

Fergana: revenue, operating expenses and gross margins



Source: Larson, D., D. Khidirov & I. Ramniceanu, 2015. "Uzbekistan: Strengthening the Horticulture Value Chain," World Bank Other Operational Studies 21495, World Bank.

The International community and CSOs have raised concerns about the practice of using forced and child labor for cotton harvesting. The World Bank, in consultation with the government and development partners, has adopted a multi-pronged approach to address child and forced labor issues in Uzbekistan. These include (i) pursuing continuous country dialogue and collaboration with international/multilateral agencies and donors to address these issues; (ii) performing sector analytic work and policy dialogue to promote diversification away from cotton and mechanization of cotton harvesting; (iii) strengthening project-level mitigation measures and binding provisions, including implementing a Third Party Monitoring (TPM) and Feedback Mechanism (FBM) to help address child and forced labor issues in connection with the project activities or within the project area; and (iv) promoting crop diversification and intensification, and supporting agricultural mechanization through a number of investment operations. This comprehensive effort to address the issue of child and forced labor in cotton harvesting has received wide support and endorsement from development partners and community based organizations.

The sustainability challenge

This section has shown

1. Water, agriculture and land use are at threshold levels of use.
2. Energy provision and use inefficiencies are extremely costly to the economy
3. Uzbekistan is poorly connected internally and externally

This section raised some questions

1. How could agricultural diversification reduce the burden on scarce water resources?
2. What investments would be needed to improve energy efficiency?
3. How could connective infrastructure improve (i) service delivery (ii) trade (iii) labor mobility?

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Selected policy questions

Given the diagnostic above, what policies and/or investments would yield the highest returns in terms of:

- (i) Employment creation and productivity growth?
- (ii) Opportunities for those at the bottom of the income distribution economic?
- (iii) Social and environmental sustainability?

The SCD Analysis proposes the following areas of focus:

Sectoral Policies

- Incentivize firm growth and hiring through reforms to tax and monetary policies
- Promote agricultural diversification and modernization
- Invest in connective infrastructure and public goods
- Develop skills and human capital

Cross-cutting Areas

- Continuing focus on improving the investment climate and promoting e-governance
- Make the foreign exchange and access to cash certain
- Gender inclusion
- Efficient use of natural resources

Selected policy questions (2)

Improve the investment climate and nurture private sector development

Despite improvements on the regulatory side, incentives remain skewed against greater private sector participation and formalization.

A policy reform agenda would entail:

1. Promoting ‘healthy competition’

- 1. Further regulatory reforms with focus on implementation and investor protection*
- 2. Changes to tax policy to incentivize firm growth and formal hiring*
- 3. SOE reform (governance improvements and/or gradual divesture)*

2. Removing barriers to trade and technology transfers

- 1. Lowering tariffs and non-tariff barriers, including foreign exchange restrictions*

3. Improving the potential for the financial sector to allocate resources optimally

- 1. Gradually removing directed credit*
- 2. Making the access to cash certain*
- 3. Further promoting SME access to finance (including alternatives to banks)*
- 4. Further improving the financial infrastructure (change the secured transactions system accordingly to the best practice and built the credit bureau with reputable international vendor)*

4. Increase state provision of public goods

- 1. Building and maintaining key public infrastructure*
- 2. Support knowledge absorption and innovation*

Selected policy questions (3)

Promote agricultural diversification and modernization

Agricultural development remains critical to the growth / employment agenda, but the potential of Uzbekistan's agriculture is under-exploited... with specific issues regarding labor deployment.

A diversification / modernization agenda would entail:

1. Improving water use efficiency / irrigation

1. *Policies*
2. *Technologies*
3. *Infrastructures / Investments*

2. Leveraging technological innovation for raising productivity

3. Promoting diversification into horticulture and livestock

4. Developing agro-industrial value chains

1. *Infrastructure development (storage, irrigation, transport)*
2. *Investment promotion (loans, direct, mobilization of other investors)*
3. *Technical assistance (training, safety standards, environmental and social ecosystems protection)*

Selected policy questions (4)

Invest in connective infrastructure and public goods

Investments in key infrastructure and connectivity would support growth, inclusion and sustainability.

Strategic investments could focus on:

1. Productive infrastructure

Key priority areas include:

1. Critical power and district heating infrastructure
2. Irrigation infrastructure

2. Connective infrastructure

Key priority areas include:

1. Trade facilitation infrastructure
2. Road and rail networks
3. ICT

Selected policy questions (5)

Develop skills and human capital

While Uzbekistan is doing well already there is scope to focus more on those most vulnerable: (i) the youth and women still unable to make the most of labor market opportunities (ii) those left behind of the growth process.

A promotion / inclusion agenda would entail:

1. Building human capital and skills

Key priority areas include:

1. Expanding access to quality ECD
2. Modernizing curricula
3. Improving access to post-secondary education

2. Improving safety nets and social protection

Key priority areas include:

1. Active labor market programs with focus on discouraged workers and women
2. A gradual move to poverty targeted welfare programs

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Next steps

1. Online consultation till end August 2015
2. Preparation of SCD report in September 2015
3. Preparation of Country Partnership Framework
October 2015

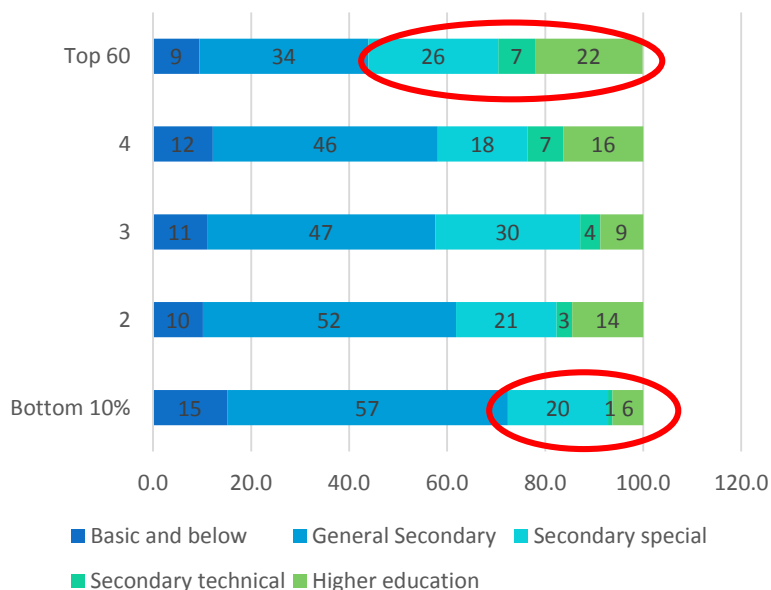
ANNEXES

Salient features: jobs –drilldown (cont.)

Welfare also appears to be determined and perpetuated by differences in access to post secondary education

Household welfare is strongly correlated with post-secondary education ...

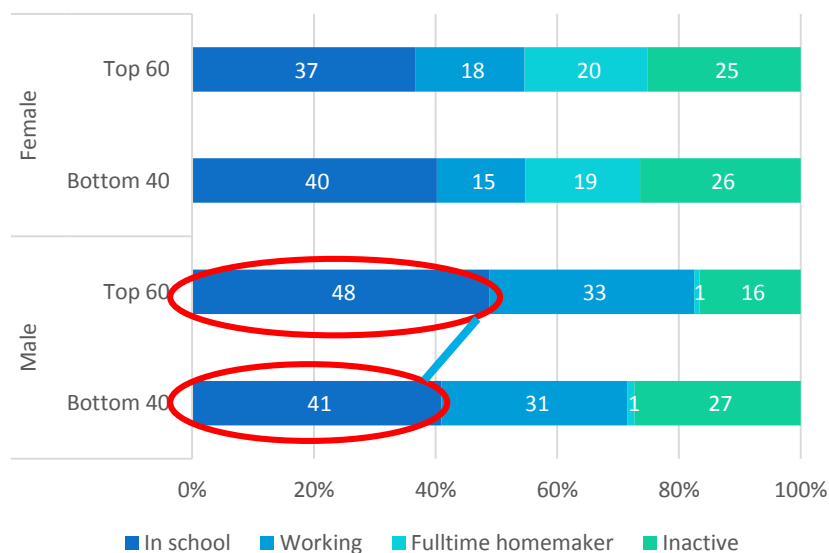
In percent of household HEADS per decile



Source: WB Calculations using CALISS

as is the likelihood of children staying in school longer

What activities are 16-22 year olds doing?



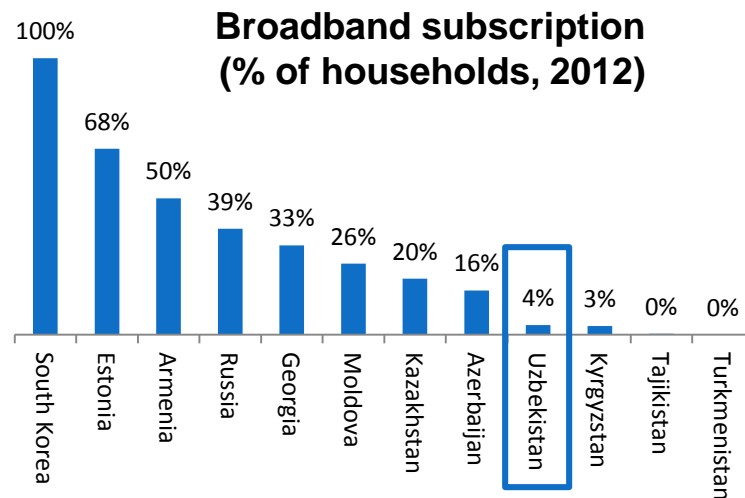
Source: WB Calculations using CALISS

Though unobserved, variations in access could also be compounded by differences in the quality of education received

Salient features: internal connectivity

ICT: e-services has significant potential, but is mostly limited to urban areas

- Government e-service initiatives are addressing the transparency of public services and reducing transaction costs
- However only about 30% of population uses the Internet, and broadband use (only 4%) is limited to key cities; affordability is also poor (1 Mbps internet = 2 x annual income, 2011)



Source: ITU, 2012

e-Government Ranking (UN e-Government index, 2012)

1 Republic of Korea
5 USA
27 Russia
38 Kazakhstan
91 Uzbekistan
96 Azerbaijan
99 Kyrgyz Republic

Source: UNDESA, 2012