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INTERNATIONAL MONETARY FUND

Minutes of Executive Board Meeting 18/40-1

10:00 a.m., May 4, 2018

1. Republic of Uzbekistan—2018 Article IV Consultation

Documents: SM/18/89 and Supplement 1, and Supplement 1, Correction 1, and Supplement 2

Staff: Jaeger. MCD; Zeidane, SPR

Length: 35 minutes

Executive Board Attendance

T. Zhang, Acting Chair

Executive Directors	**Alternate Executive Directors**
M. Mkwezalamba (AE)	
	M. Raghani (AF)
	B. Lischinsky (AG), Temporary
H. Jang (AP)	
	M. Coronel (BR), Temporary
	P. Sun (CC)
	A. Del Cid-Bonilla (CE), Temporary
	M. Sylvester (CO), Temporary
M. Erbenova (EC)	
	A. Castets (FF)
	S. Maluck (GR), Temporary
	M. Roy (IN), Temporary
	M. Psalidopoulos (IT)
	Y. Saito (JA)
J. Mojarrad (MD)	
	F. Al-Kohlany (MI), Temporary
	D. Cools (NE), Temporary
T. Ostros (NO)	
	L. Palei (RU)
	F. Rawah (SA), Temporary
	K. Sumawong (ST), Temporary
M. Panek (SZ)	
	T. Hemingway (UK), Temporary
	P. Pollard (US), Temporary

T. Rumbaugh, Acting Secretary
H. Malothra, Summing Up Officer
O. Bespalova, Board Operations Officer
L. Nagy-Baker, Verbatim Reporting Officer

Also Present
European Central Bank: T. Persico. Information Technology Department: F. Gheriss. Legal Department: C. Blair, N. Rendak. Middle East and Central Asia Department: A. Jaeger, A. Mazarei. Strategy, Policy, and Review Department: Z. Zeidane. Alternate Executive Director: C. Barron (AP), P. Inderbinen (SZ), G. Johnston (AP). Senior Advisors to Executive Directors: Y. Danenov (SZ), J. Shin (AP), E. Sishi (AE). Advisors to Executive

1. REPUBLIC OF UZBEKISTAN—2018 ARTICLE IV CONSULTATION

Ms. Barron and Mr. Kim submitted the following statement:

On behalf of our Uzbek authorities, we thank staff for the constructive discussions and candid assessment of Uzbekistan's short- and medium-term challenges and perspectives, against a background of ongoing reforms. Uzbekistan faces challenges but also opportunities. The new government is pivoting toward a more open and market-oriented development model, and reigniting long-delayed reforms. The authorities broadly concur with staff's assessment of the economic challenges and their policy recommendations.

Economic Developments and Outlook

In February 2017, the new government initiated a comprehensive reform program with the adoption of the National Development Strategy for 2017-21. This strategy reiterated the authorities' commitment to ensuring macroeconomic stability, improving the quality of life of households, and achieving inclusive growth, especially in rural and remote areas of the country. The Strategy includes five priority areas: improving public administration and state-building; ensuring the rule of law and judiciary reform; maintaining economic growth and liberalizing the economy; enhancing social safety nets; and ensuring security and implementing a constructive foreign policy.

Under this development strategy, robust growth and job creation are expected to continue. Economic growth slowed from 7.8 percent in 2016 to 5.3 percent in 2017 due to FX adjustments, but strong investment has remained a key driver of growth. During 2018-19, the authorities expect economic growth to be around 6 percent, supported by favorable external demand and commodity prices, a pickup in agriculture due to reform measures and the normalization of harvests, and a buoyant construction sector building houses and public infrastructure. The authorities intend to conduct tighter fiscal and monetary policy to help control inflation, which is expected to remain elevated as newly-liberalized prices continue to adjust.

Exchange Rate Policy

A key economic reform was the liberalization of foreign exchange regulations in September 2017. The authorities unified the official and parallel market FX rates, depreciating the official exchange rate by 50 percent. As a result, individuals and entities can freely buy and sell foreign currency, and the requirements for compulsory sale of foreign currency by exporters have been removed. The exchange rate is now determined by the market.

Monetary Policy

The Central Bank of Uzbekistan (CBU) has taken considerable steps to improve its monetary and exchange rate policies. Monetary policy was tightened before the start of the FX market reforms and the CBU has been able to effectively manage anti-inflationary policies and ensure the stable functioning of the banking system during this period of liberalization. Starting in 2018, the CBU has been implementing a new strategy based on the principle of foreign reserves neutrality. This aims to sterilize additional liquidity from the CBU's direct purchase of gold by supplying the appropriate amount of FX into the market. The CBU has also continued to take active steps in employing interest rate instruments. Use of these monetary policies has resulted in a deceleration of money supply growth, a stabilization of interest rates in the interbank money market, an increased propensity of households to save in national currency, and a stabilized exchange rate. The CBU has declared its intention to switch to inflation targeting in the medium term, as staff recommend. Technical assistance from the Fund has been particularly valuable in improving the CBU's capacity in areas such as monetary policy operations and interbank market development, designing the interim monetary policy regime, compiling balance of payments data, and stress testing.

Fiscal Policy

Despite the challenges of reform, the authorities have continued their efforts to maintain a prudent fiscal policy, and tax reform is a top priority. The authorities will conduct a tighter fiscal policy by reducing on-lending operations. They will also focus budget spending on mitigating the impact of the exchange rate adjustment on the vulnerable, supporting critical public enterprises to gradually converge toward greater sustainability and cost recovery, and sustaining the public investment program. The authorities have made significant efforts to consolidate on- and off-budget transactions in the fiscal data. They have recently launched tax reforms to improve the tax system and tax administration. This process envisages reducing the difference in tax burden between small and large business entities, rationalizing of the VAT rate, unifying and cancelling a number of taxes and mandatory payments, and improving tax administration procedures. The authorities have also begun efforts to transform the customs and pension systems.

Structural Reforms

The authorities remain committed to their goal of achieving upper-middle-income status by 2030, by increasing the economy's competitiveness, improving the business environment, and developing the infrastructure to support rapid job creation. Broad structural reforms began in 2017. These included the FX market reforms, liberalization of the visa regime, more independence for the CBU, an assessment of banking sector resilience, the implementation of financial recovery plans in key SOEs, plans to resume the accession process to the WTO, and new legislation to promote competition and public-private partnerships. The recommendations of the consulting group on SOE governance will be ready in July, providing an opportunity to draw up a comprehensive plan to deal with SOE issues. The authorities expect the suite of reforms to result in greater macro-fiscal and financial resilience, new markets and more private sector participation. They will help improve the business climate and increase the competitiveness of the economy in order to create new jobs for a rapidly increasing population, especially among youth. The authorities are also working on creating greater economic data transparency, including by joining the General Data Dissemination Standard.

Mr. Fachada and Mr. Coronel submitted the following statement:

We thank staff for the report and Ms. Barron and Mr. Kim for their statement. We welcome the opportunity to discuss Uzbekistan's Article IV consultation, after a lapse of almost three years. We are encouraged by the measures adopted since last year by the new government to open up and liberalize the country's economy.

Real GDP growth over the period 2007-2016 was among the highest in the world. The authorities pursued prudent fiscal policies, strengthened Uzbekistan's external position, and accumulated significant foreign reserve buffers. Progress on poverty reduction was also significant, although the fast demographic transition posed important challenges. Indeed, the rise of the country's working-age population has outpaced by far the economy's capacity to create jobs in recent years.

Transitioning to a market-oriented growth model is both a challenge and an opportunity to Uzbekistan. With the drivers of the old central planning system and government-led growth model exhausted, the new authorities have embarked on reforms aimed at creating a market-oriented economy, underpinned by private sector investment. Against this background, we welcome the authorities' emphasis on ensuring macroeconomic stability and improving the business climate, including initiatives to, inter-alia, rationalize public administration, ensure the rule of law, reform the judiciary, liberalize prices and the foreign exchange market, modernize the financial sector, and strengthen social safety nets.

This ambitious reform agenda should be gradual to avoid political or capacity setbacks. The far-reaching reform agenda also encompasses fiscal transparency, with the elimination of off-budget transactions, restructuring of state-owned enterprises, and reduction of inefficiencies in legacy industries. In parallel with these changes, we welcome staff's recommendation for a revenue-neutral, comprehensive tax reform. We also commend the intention of the authorities to increase data transparency, including by joining the IMF's enhanced General Data Dissemination Standard (e-GDDS). Although many of the reforms have already been introduced—most notably the liberalization of the foreign exchange market—we agree with staff on the need to build-up a critical mass of experience and institutional capacity to avoid risks of setbacks.

Monetary policy should be adjusted to contain inflation pressures. As a result of prices and foreign exchange liberalization amid relatively loose fiscal and monetary conditions, inflation spiked to nearly 20 percent in 2017. A tighter monetary and fiscal stance should contribute to bring inflation down to one-digit levels by 2019. We concur with staff on the need to bring real policy rates to positive territory, enhance the capacity of the central bank to conduct open market operations, and eliminate distortions in the credit market. As staff, we believe the authorities should create adequate conditions—including strengthening central bank independence—before moving to an inflation targeting framework.

Mr. Doornbosch and Mr. Cools submitted the following statement:

We welcome the renewed opportunity for the Board to discuss the Uzbekistan Article IV consultation, and we thank staff for the insightful report and Ms. Barron and Mr. Kim for their buff statement. We concur with staff's positive appraisal of the impressive reforms deployed by the authorities, as they are transitioning Uzbekistan from a state-driven growth model to a free market economy. We invite the authorities to keep up the current reform momentum.

For these reforms not to lose pace in the medium term, it is essential that the reform agenda continues to garner broad public support. In this light, we welcome the mitigating measures that accompany the necessary policies of fiscal and monetary tightening. Given the strong increase in the working age population, we particularly commend the authorities' active labor market programs, including those aimed at improving the employability of the longer-term unemployed.

While we recognize that poverty has been on a strong downward trajectory for years (UNDP quotes official government statistics showing a reduction of poverty levels from 27.5 percent in 2001 to 12.8 percent in 2015.), we invite staff to continue closely monitoring the distributional effects of the reform program. Potentially persistent high inflation resulting from the liberalization of the FX market and the liberalization of price policies should be met with monetary and fiscal tightening. At the same time, bank credit might tighten due to funding gaps and a deterioration of bank asset quality. As a result, lower and middle-come segments of society could see their purchasing power reduced. This could potentially erode support for further reforms.

We also welcome the authorities' efforts to ensure an efficient and arms' length allocation of credit. However, we agree with staff that further work remains to be done. Stricter limits should be put on the FRD's on-lending activities.

Finally, we wonder which additional measures could be taken to improve the de facto independence of the central bank. We would also be interested to hear why the authorities have not yet consented to the publication of the staff report.

Mr. Sun and Ms. Lok submitted the following statement:

We thank staff for the insightful report and Ms. Barron and Mr. Kim for the informative buff statement. Since last year, Uzbekistan has embarked on a comprehensive reform program to build an open and market-oriented economy and promote inclusive growth. As the authorities continue to implement the program, we encourage them to stay vigilant against possible complications and risks that may arise during the process. We broadly agree with the thrust of staff's appraisal and wish to make the following points for emphasis.

We believe the authorities should maintain a prudent fiscal policy stance, which has kept public debt low, and will help preserve a healthy fiscal position to meet potential costs that may result from the ongoing restructuring of state enterprises and the banking system. Like staff, we support the authorities' plans to tighten fiscal policy via lending cuts this year to rein in inflation. We also welcome the increased social safety net spending and labor market programs, which would help contribute to more inclusive growth. We encourage the authorities to improve fiscal transparency, and take positive note that progress has been made in consolidating on- and off-budget transactions in reported fiscal data.

A resilient banking system will help the economy weather challenges that may arise from weakening profitability of state-owned enterprises amidst restructuring and economic reforms. We share staff's view that going forward, banks should seek more market-based solutions for funding as an alternative to the Fund for Reconstruction and Development. We support the recent reforms to the banking system, and look forward to further steps to promote the stable development of a sound financial sector, which in turn, could contribute to broader economic growth. In the Authorities' Views, it was noted that foreign banks generally found it difficult to operate in the region. In staff's view, what can be done to raise attractiveness of Uzbekistan to foreign banks?

Further structural reforms are needed on various fronts, and we welcome the authorities' continued commitment to a wide-ranging set of reforms, including the plan to address SOE issues in a comprehensive manner based on the forthcoming recommendations on SOE governance. As suggested in the staff report, some reforms, such as the liberalization of prices and reduction of monopolistic practices, need to go hand in hand to be effective. Careful planning and sequencing are therefore critical, and we encourage the authorities to seek technical assistance and advice where needed to create synergies across reforms and ensure smooth implementation.

While the authorities have made significant efforts to improve the quality and availability of economic data, as noted in the Informational Annex, shortcomings remain. We believe the authorities should further step up their efforts to enhance data quality, not only to facilitate better surveillance, but also to ensure well-informed policymaking. To this end, we welcome the authorities' agreement to participate in the enhanced General Data Dissemination System.

Reform is no easy feat. Uzbekistan has achieved notable progress since the 2015 Article IV consultation, including the liberalization of the foreign exchange market. We wish the authorities every success in pressing forward their efforts, while striving to mitigate risks, build capacity, and ensure inclusiveness of growth.

Mr. Castets and Ms. Van Hoek submitted the following statement:

We thank staff for the documents as well as Ms. Barron and Mr. Kim for a helpful buff statement. Uzbekistan is at a crucial moment, with the recent implementation of several reforms transforming its economic model from a state-driven growth model resulting in a segmented economy, towards a more open and market-oriented economy. Such a profound transformation comes with many challenges, but Uzbekistan can benefit from the experiences of previous transitions, which show that drawbacks, although hardly avoidable, can be overcome and even used as catalysts. In this regard, the sequencing of reforms is paramount and we encourage the authorities to mobilize the Fund's analytical capacity in support to the design of an appropriate and realistic reform agenda. We share the thrust of staff's appraisal would like to make the following comments for emphasis.

We commend the authorities for liberalizing the foreign exchange regulations last September. We share staff's view that controlling inflation (currently at a high level of 20 percent) is a priority in the short term and that it should be done through a tightening of monetary policy. The Central Bank of Uzbekistan (CBU) did tighten its monetary policy in preparation of the exchange rate liberalization but has since maintained stable nominal exchange and refinancing rates. The staff's input on the reasons behind this policy choice and the weakness of monetary policy transmission channels in Uzbekistan are welcome. While we note staff's medium-term recommendation to progress towards inflation targeting, using a broader range of indicators appears as a more realistically achievable objective in the short term and we support staff's recommendation in that regard.

Uzbekistan's economy is also characterized by ample fiscal space. Its public debt stands at 24.5 percent of GDP and the Debt Sustainability Analysis qualifies the risk of external debt distress as low, including in shock scenarios. However, authorities seemed to have made a limited used of the existing fiscal space to counterbalance the warranted tightening of the monetary policy and its impact on growth and on the most vulnerable. Furthermore, the budget support has been provided mostly through an increase of net lending by the FDR which impact is difficult to assess. Can staff please share its views on the recommended policy mix balance between budgetary support and tighter monetary policy and on the most effective budgetary channels in its view? In addition, the report is silent on the social impact of such a depreciation of the exchange rate on the population, notably the most vulnerable, and the adequacy of the strengthening of the social safety nets. The staff's comments are welcome.

We commend the authorities for their efforts to improve the quality of the economic data and encourage them to continue to work in that direction. The selected economic indicators (table 1) show a significant drop in the GDP per capita expressed in U.S. dollars between 2016 (2,094) and 2017 (1,491). Even though this evolution can be explained by the devaluation, the figure for 2017 still seems low. Could staff comment on the presented figures and on whether a GDP rebasing exercise is considered by the authorities?

Finally, we take note that the authorities took steps to improve the business environment in line with Fund's recommendations to reform the investment climate. Can staff please elaborate on the implemented measures? We would also appreciate staff's view on the issues of governance and corruption in Uzbekistan which are not mentioned in the report.

With these remarks, we encourage the authorities to publish the Article IV report as it would be an important signal of their willingness to progress towards a more open economy.

Mr. Ostros and Mrs. Jekabsone submitted the following statement:

We thank staff for the report and Ms. Barron and Mr. Kim for the informative buff statement. We welcome the first steps of opening up and liberalization of the Uzbekistan's economy bringing about challenges and opportunities of the transition. Given the country's youthful and growing workforce and abundant natural resources, Uzbekistan has a strong potential to catch-up with the living standards of the regional peers and become economic hub of the region if the challenging reform agenda is persistently pursued. We are encouraged by the president's development strategy to advance the critical areas of the economy that will require political will and strong ownership. We broadly share staff's assessment and would like to offer the following comments for emphasis.

We share staff's view that a tighter monetary stance will help to lower inflation, including by raising the refinancing rate and reducing the accumulating FX reserves. Moreover, the envisaged medium-term shift to inflation targeting needs to be supported by increasing the central bank's de facto independence.

We believe that the authorities' primary focus of the reforms and measures needs to be on job creation to accommodate around half a million new entrants into the labor market annually, and to reduce further emigration. We emphasize the need for wide-ranging structural reforms to warrant the restructuring of state enterprises, improve business environment, and fight corruption, which is critical for the strengthening of the private formal sector, attraction of FDI, and job creation. Moreover, while some progress has been achieved, the authorities should take concrete steps to reduce monopolistic practices, ease access to finance, liberalize trade, and promote competition. Renewed talks for the accession into the WTO is a step in the right direction.

We support staff's call for gradual, revenue-neutral and comprehensive tax reform to reduce the segmentation of companies, simplify the tax system, and reduce tax burden to encourage expansion of the private sector and support job creation. It is also necessary to boost tax revenues to offset expected revenues decline from state enterprises as a result of policies shift, and provide resources for the implementation of the Sustainable Development Goals.

Mr. Merk and Mr. Maluck submitted the following statement:

We thank staff for an informative report and Ms. Barron and Mr. Kim for their helpful buff statement.

We broadly concur with the staff's assessment. We agree with staff that Uzbekistan has initiated far-reaching reforms aiming at becoming a more open, market-oriented economy. Having said this, significant challenges remain. Lasting ownership by the authorities is needed. At the current juncture, bringing down the high inflation fueled inter alia by the recent exchange rate depreciation deserves high priority. The demographic situation with a high share of working-age population calls for efforts to create jobs.

Regarding the external sector assessment, staff identifies a current account gap of about 6 percent. The gap is larger than in recent years, with the actual current account and the EBA norm deviating from their 2016 levels to a similar degree but in opposite direction. The staff indicates that an upward bias may affect the reported current account surplus. Moreover, we agree with the staff's appraisal that the large depreciation in September 2017 suggests that the external position was not as strong as suggested by the EBA model. We would appreciate further information on the factors leading to the change in the current account norm estimated by staff.

While public debt remains at sustainable levels, we encourage the authorities to further strengthen debt transparency. We welcome the authorities' commitment to bring all fiscal operations on-budget starting in 2019. Potential fiscal costs related to restructuring state enterprises might be substantial. Given that many state enterprises' revenues are primarily in domestic currency, large FX exposures from government on-lending pose a non-negligible risk.

We broadly share staff's overall assessment of reserve adequacy. We note that assets of the Fund for Reconstruction for Development (FRD) are included in the reserve metric but are not considered available to insure against external shocks or for central bank FX operations. Could staff elaborate on why these assets are included in the reserve metric anyhow?

Regarding monetary policy, the authorities should focus on bringing down inflation and further tighten the monetary policy stance. Both exchange rate pass-through and loose monetary policy in the first half of 2017 have contributed to rising inflation rates. While tradable goods seem to be the main inflation driver, prices of non-tradables are also increasing. This may indicate a delayed adjustment to tradables, which would suggest prolonged high inflation. We therefore share staff's assessment that a further tightening of monetary policy is appropriate. Moreover, we agree with staff that de facto central bank independence is a prerequisite for effective inflation targeting as envisaged by Uzbek authorities. We would therefore welcome additional comments on how central bank independence has evolved de jure and de facto in the course of reforms.

Regarding Art. VIII obligations, we welcome the elimination of two exchange restrictions and a multiple currency practice. We welcome staff's intention to closely monitor ongoing implementation.

While early structural reforms send positive signals to investors, more action is needed to effectively improve the investment climate. We welcome efforts to reduce segmentation of the economy and revoke privileges of state enterprises. Legacy issues of state enterprises must be addressed as soon as possible in the transition process. Monopolistic practices should be reduced and competition in the domestic market promoted. We agree with staff that tax reform could remove disincentives for small enterprises to grow, and stimulate job creation but should be revenue neutral and gradual.

We appreciate efforts of the Uzbek authorities to enhance data collection and dissemination, which is crucial for effective surveillance and policy analysis. We encourage the authorities to consent to the publication of the staff report. We take note that both the last and the present Article IV consultations have been delayed. Could staff provide information on the reasons for repeated delays in completing Article IV consultations with Uzbekistan?

Ms. Pollard and Mr. Rudolph submitted the following statement:

We welcome the opportunity to discuss the Article IV for Uzbekistan, the first since 2015 and commend the new government for the steps taken thus far to tackle Uzbekistan's longstanding economic and social challenges. We appreciated the buff statement by Ms. Barron and Mr. Kim, noting that "the new government is pivoting toward a more open and market-oriented development model, and reigniting long-delayed reforms." Given how deeply entrenched the old system is, the reform process will inevitably meet resistance from powerful vested interests, but the authorities are off to an excellent start. We agree with staff that the authorities need to "adhere to their reformist vision, persevere in the face of setbacks, and communicate clearly."

Exchange Rate System

We commend the authorities for ending the exchange restrictions and multiple currency practice through unification of the official and parallel market exchange rates and improving access to foreign currency. These steps were a clear indication that the new government intends to move toward a more open economic system. We encourage the authorities to increase the extent to which they allow the currency to move in line with economic fundamentals, which should reduce the overvaluation of the currency and improve competitiveness.

Structural Reforms

It is difficult to overstate the amount of economic reform work to be done after a long history of a state-controlled, closed economy. Nevertheless, the new government has taken several key initial steps. We encourage the authorities to continue this positive momentum. We appreciated staff's attention to reform risks and lessons learned from earlier transitions, which can help guide Uzbekistan's reform process.

Governance

The process of rooting out decades of corruption will be long and hard, but we are encouraged by the authorities' commitment. A particularly welcome governance reform is the establishment of a website for citizen grievances, which will help shine a light on the public sector. We are encouraged to see that one of the five priority areas in the National Development Strategy centers around enforcing the rule of law through an independent judiciary. Among the macro-critical channels identified in the recently updated Fund framework for engagement on governance, the rule of law will be particularly important in Uzbekistan, and we hope enhanced staff work in this area will be a valuable resource to the authorities as they embark in this direction.

Diversification

While the cotton and energy industries offer valuable resources for Uzbekistan, the economy will need to diversify into sectors with higher human capital content if the country is to make full use of its demographic dividend. As liberalization continues, there should be a price discovery process that will reveal industries in which Uzbekistan enjoys comparative advantages, and we wish the authorities the best of luck as they transition towards a more dynamic economic model that allocates resources based on these valuable price signals.

Transparency

Enhancing transparency will help improve governance and economic surveillance. We welcome the steps underway to increase fiscal transparency by bringing all transactions on budget. Improving data quality and availability should be a priority. We welcome the authorities' commitment to participate in the enhanced General Data Dissemination System and the technical assistance provided to help in this regard. We encourage the authorities to consent to publication of the Article IV report as a further indication of their commitment to greater openness and transparency.

Mr. Hurtado and Mrs. Del Cid-Bonilla submitted the following statement:

We thank staff for its report and Ms. Barron and Mr. Kim for their informative buff statement. We welcome the comprehensive reform agenda launched by the government to modernize the economy towards a more open and market-oriented model that will improve living standards and stimulate job creation. Uzbekistan's solid growth trajectory and strong external position open a window of opportunity to vigorously impulse planned reforms. We commend the authorities for the reforms already introduced, particularly the liberalization of the FX, tariff adjustments and plans to resume the accession process to the WTO. As staff pointed out, the magnitude of the needed reforms is large, and their success will largely depend on social adherence to the new vision, strong perseverance and clear communication. We broadly concur with staff's assessment and would limit our comments to a few points.

Keeping macroeconomic stability is fundamental to move on with the reform agenda. In this regard, we agree with staff that a tighter monetary policy (MP) is needed to bring inflation down. However, we see some differences between staff's policy advice and the strategy being pursued by the authorities. For instance, while staff recommends an additional increase in the nominal refinancing rate and halting FX accumulation by introducing a regular pre-announced program of FX sales from the CBU's gold purchases, the authorities consider that the current level of the refinancing rate is appropriate and have adopted a neutrality principle which means gold purchases and sales would be equal. Could staff clarify this apparent difference in criteria and therefore how the CBU intends to tighten MP? Could staff also indicate which operational tools does the CBU have currently available and what the specific TA recommendations are to strengthen the existing toolkit?

Prudent Fiscal policy is an important component of macroeconomic stability. The fiscal deficit increased from 0.6 in 2016 to 3.3 in 2017, mostly attributed to the amount of loans extended by the Fund for Reconstruction and Development (FRD) to state enterprises (SEs) and for state banks' recapitalization; by the same means, the bulk of the fiscal adjustment in 2018 would mainly come from a cut in FRD lending operations. We would like staff's clarification on why these loans are treated as expenditures and if the authorities have adopted a broader policy to limit the amount of FRD loans to SEs. We also would like to understand better the budget classification of expenditures presented in Tables 4 and 5, in particular, which of those are mainly wages.

The banking system indicators are sound, but the highly concentrated portfolio in SEs is a source of vulnerability. Banks' assets quality can deteriorate quickly if SEs' profits decline and because many SE loans are in FX. We welcome the authorities' intentions to reform the banking system. Steps taken to reduce administrative costs and strengthen banks' governance go in the right direction. However, the system will need a far-reaching modernization plan to improve its competitiveness, efficiency and intermediation role. This plan should include the transformation of state banks' business model to a more commercially-oriented one, including mergers and privatization options, strong regulatory and supervisory frameworks, a bank resolution framework based on best practices and international standards to reduce moral hazard and an effective lender of last resort mechanism. Could staff elaborate on the plan contemplated in the authorities'?

We concur with staff that addressing balance sheet strains and restructuring state enterprises should be key priorities in the transition and we highlight the importance of promoting competition from the very first stages of reform. We commend the work of the consulting group regarding SEs governance, which could provide the basis to elaborate a comprehensive plan to deal with SE issues. In our view, a comprehensive plan regarding SE's cannot disregard privatization options and we encourage the authorities to take this into account.

Finally, we congratulate the authorities for their efforts to increase economic data transparency, including the preparation of a roadmap to improve statistics, to be released in November 2018, and their decision to join the IMF General Data Dissemination Standards.

Mr. Alkhareif and Mr. Keshava submitted the following statement:

We thank staff for a focused report and Ms. Barron and Mr. Kim for their helpful buff statement. We are in broad agreement with the staff's assessment and policy recommendations and would limit our remarks to a few issues.

We welcome the launching of far-reaching reforms under the National Development Strategy (2017-21), which aim at building a more open and market-oriented economy. It is also reassuring that Uzbekistan has initiated reforms from a position of strength with large external buffers, and low and sustainable public debt. We are encouraged to note that these reforms could have positive regional spillovers, given Uzbekistan's sizable population and geographic location. In this connection, it would be important to persevere with the reform agenda and benefit from the lessons from earlier transition experiences to address emerging challenges.

The authorities' plans to tighten fiscal policy in 2018 by reducing on-lending operations is appropriate to help reduce inflation. In this connection, we encourage the authorities to continue their efforts over the medium term to restrain on-lending operations. We welcome the emphasis placed by the authorities on increasing fiscal transparency and look forward to further progress in the period ahead. The staff has rightly underlined the need for undertaking tax reform, along with the improvements in tax administration, to help in terms of job creation for a rapidly increasing population while ensuring revenue-neutrality to meet the stated goal of improving education, health care, infrastructure, and the social safety net under the new development strategy.

We take positive note of the central bank's plan to pursue a tighter monetary policy stance to bring inflation to single digits. In the financial area, while the banking system is well-capitalized and profitable, staff has noted that banks will likely face challenges related to deteriorating asset quality and low operational efficiency. In this regard, we are reassured to note that the central bank plans to further upgrade its supervisory capacity and intervention tools, including by incorporating stress testing more fully in the supervisory process.

Finally, the authorities deserve to be commended for their structural reform efforts, including to unify exchange rates and eliminate measures inconsistent with Article VIII obligations. We look forward to continued progress in enhancing the investment climate and increasing the economy's competitiveness.

With these remarks, we wish the authorities further success.

Mr. Saito and Mr. Komura submitted the following statement:

We thank staff for the comprehensive reports and Ms. Barron and Mr. Kim for their informative statement. Working-age population has increased over the last two decades in Uzbekistan, reflecting the sharp drop of mortality and fertility rates. The demographic transition makes job creation a top priority. In this regard, we support that Uzbekistan aims at opening and liberalizing the economy to demonstrate its high potential. We encourage the authorities to draw lessons from earlier transitions and closely communicate with staff in pushing reforms further. As we broadly agree with the thrust of staff's appraisal, we make some comments for emphasis.

Monetary Policy

Tightening monetary policy would be appropriate to contain inflation. Inflation peaked at about 20 percent in early-2018, reflecting loose monetary and credit policies and pass-through from FX and price liberalization. As additional liberalization of prices, especially energy prices, is planned in 2018, we agree with staff and the authorities that a tighter monetary stance is warranted. In this regard, close communication with staff is vital for the authorities to determine a pace or timing of tightening, depending on progresses in price liberalization and more broadly, economic situation.

Financial Sector

Uzbekistan needs to safeguard financial sector stability in the short term and establish a growth-supporting banking system in the medium term. While several indicators, including regulatory capital to risk-weighted assets and non-performing loan ratio, illustrate a soundness of the banking system, Uzbekistan faces challenges due to high loan concentration to state enterprises and loan dollarization. In this regard, we welcome recent reforms, such as a presidential decree instructing officials to refrain from pressuring banks to provide credit at preferential terms to selected borrowers, and further plans to upgrade its supervisory capacity and intervention tool. Going forward, banks will need more funding and capital to adequately support higher growth and job creation. In this regard, while we also believe that banks should rely on more market-based solutions, such as attracting foreign funding and more deposits from household, instead of FRD funds, what would be an obstacle to take the direction?

Structural Reform

We commend that Uzbekistan has initiated significant structural reforms. The reforms include liberalization of many prices, unification of exchange rates, and elimination of measures inconsistent with Article VIII obligations. While additional price liberalization, especially for energy prices, is important in Uzbekistan, the authorities should promote competition and improve business environment, which would help to boost economy and create jobs and lead to effective price adjustment.

Mr. Psalidopoulos and Mr. Persico submitted the following statement:

We thank staff for the insightful report and Ms. Barron and Mr. Kim for their buff statement. We agree with the thrust of the staff appraisal and we offer some comments for emphasis.

In order to prove effective, economic policy in Uzbekistan transition should successfully address inflation and unemployment without burdening the fiscal sector. The country is implementing an ambitious reform program to transit from a state-driven to an open economy model. Authorities should continue to address the high level of unemployment through timely structural reform and tighten monetary policy facing persistent inflation. Authorities should also take advantage of the positive benefit of the current demographic trend to promote inclusive growth.

The country needs to embrace a wide tax reform in order to support job creation while preserving social spending and promoting strategic infrastructures. Authorities should embrace a gradual and revenue-neutral fiscal reform paying attention to complement corporate taxation with proper interventions on the labor market. In sustaining strategic investment, authorities should not consider as a priority to maintain a commercial surplus, but should lift import restrictions (especially for investment-related goods).

Public debt appears sustainable, nonetheless the not-guaranteed debt of SOEs could pose an indirect fiscal pressure risk. In addition, we invite authorities to improve transparency in public finance reporting in order to avoid an unnecessary source of concerns. In this regard, we would ask staff if the reported lack of data could impact in a relevant way the current risk assessment and if the application of the new DSA framework could, again, impact the assessment.

Efforts to enhance the business environment, according with the Fund’s recommendations, are ongoing. In order to improve the business climate (due to the large share of public influence on economic activities), authorities should follow a stable medium-term public investment program as well as increase transparency and reliability of the procurement’s procedures. While we share the staff advice to pursue regional trade integration, we wonder if the referred narrative on trade specialization is fully consistent with the country’s need to promote a more diversified and private-sector-led economy. In this regard, we commend the authorities for reinitiating commitment to World Trade Organization (WTO) accession.

Authorities should tighten monetary policy to contain long-standing inflationary pressures and manage excess liquidity via positive real interest rates. While we noted the different view between staff and the Central Bank of Uzbekistan on inflation, we invite the CBU to be ready to intervene, if double digit inflation persists. We commend the authorities for their efforts to liberalize the exchange rate as well as to eliminate exchange restrictions, nonetheless we have some concerns due to the reported inflationary impact. In this regard, an increasing of the exchange flexibility constitutes an overall indication for developing countries: we wonder if in the case of Uzbekistan, it could be useful to acknowledge proper policies to mitigate potential negative effects in future policy advice. The staff's comments are welcome.

The financial sector is sound, but its concentration and segmentation poses some risks. In particular, the concentration of credit in SOEs could generate potential negative dynamics. At the same time, the role of the Fund for Reconstruction and Development should be limited as well as its FX credit share. Moreover, we invite authorities to improve both the CBU supervisory capacity and the efficiency of the banking system as it could play a key role supporting domestic and international private actors.

Finally, as the proposed Article IV consultation in 2015 should have held on the standard 12-month cycle, we would like to the ask staff the reasons for such a delay. In addition, as the discussed report (and its overall positive remarks) could constitute a useful tool to attract additional investment, we invite authorities to consider its timely publication and would like to ask the staff if any indication was provided since the circulation of the report.

Mr. Gokarn and Mrs. Roy submitted the following statement:

We thank staff for their documents on Article IV consultations with the Republic of Uzbekistan and Ms. Barron and Mr. Kim for their informative buff statement. It is encouraging that Uzbekistan has initiated significant structural reforms in 2017 and has liberalized many prices, unified exchange rates, and eliminated measures inconsistent with Uzbekistan's Article VIII obligations. However, in the process, the inflation rate has soared, necessitating tight monetary policy, and growth has slowed, with implications for the job creation necessary in the economy. Reassuringly, external sector buffers are high and fiscal indicators are favorable. We broadly agree with the thrust of the staff appraisal and have the following additional comments.

There is a considerable difference in growth and inflation projection by the staff and authorities. While growth for 2018-19 is projected to be about 5 percent by staff, the authorities are more optimistic and forecast growth to be around 6 percent. Since both the projections assume that growth will be supported by strong commodity prices and trading-partner demand, reforms that boost agriculture, and the government's housing and infrastructure programs, why is there a difference in the final projected rate?

In case of inflation projection, while inflation is projected to decline from 20 percent now to 12-14 percent by end-2018 and single digits by end-2019 by the central bank, staff project it to decline to 19.5 percent and 12.9 percent, respectively. Given that the authorities plan to tighten both monetary and fiscal policy in 2018 to reduce inflation, what other measures can the staff propose to bring down the rate of inflation, whose persistence could be detrimental to the economy by choking off economic activity?

It is encouraging that the authorities are planning to cut lending operations that fuel credit growth, saving about half of the expected additional revenues in 2018 from higher-than-projected commodity prices, improving tax administration and increasing social safety net and active labor market programs spending. If implemented as planned, these measures will reduce the augmented fiscal deficit to 1.3 percent of GDP in 2018 which will stabilize at a medium-term fiscal deficit of 2 percent of GDP by 2023 while the public debt to GDP ratio would increase to about 25 percent from 9.3 percent now. With a relatively healthy debt situation as of now, the authorities appear to have fiscal space available, even as they address the high inflationary situation. What implications would this medium-term increase in fiscal deficit and public debt have for the fiscal space and overall macroeconomic balance in the economy?

Uzbekistan's working-age population has surged over the last two decades, making the creation of more and better jobs an overarching policy priority. Past policies had little success in creating sufficient jobs or raising living standards in line with the country's need. The staff report states that the government may need to step up social expenditures (education, health) and spending on real capital (infrastructure) to take advantage of Uzbekistan's demographic window over the next two decades. The budget envisages about ¼ percent of GDP for active labor market programs to improve the employability of the longer-term unemployed. Tax reform could also help in creating jobs by removing tax exemptions for small firms wherein economies of scale could come into play. However, failure to create adequate jobs will continue to lead to greater migrant labor syndrome and socio-economic problems. Could the staff elaborate the reasons behind the stagnation in job creation? What is the staff assessment of Uzbekistan's institutional and human capacity which will help it to reap the demographic dividend? Also, in addition to providing jobs, how do the authorities plan to ensure safety and security of labor in the workplace, both domestic and migrant? Could staff comment on the possible use of available fiscal space in this domain?

As the forex market is opening up, there is a greater need to ensure the stability of the market through appropriate policy measures. The staff report states that the authorities plan to proceed cautiously on lifting present restrictions on capital flows. What is the nature of controls on capital flows that Uzbekistan has in place and could they be supplemented effectively by macro-prudential measures?

Mr. Agung and Mr. Sumawong submitted the following statement:

We thank staff for a comprehensive set of reports and Ms. Barron and Mr. Kim for their helpful buff statement. While the Uzbek economy has remained resilient amidst a series of external shocks that began in 2014, the country's economic growth began slowing in 2017. Medium-term growth is also projected to moderate further with high inflation. Could staff comment on factors contributing to the substantially lower medium-term growth projections compared to the 2015 Article IV consultation? In addition, the economy is segmented and job creation remains subdued despite the growing working-age population. Against this background, we commend the Uzbek authorities for recent reform initiatives aimed at promoting sustainable and inclusive growth. We broadly agree with the staff appraisal and limit our comments to the following points for emphasis.

We agree that macroeconomic policies should aim at bringing down inflation. We are encouraged by the Central Bank of Uzbekistan's (CBU) move to tighten the monetary stance before implementing foreign exchange market reforms in September 2017. We note positively the CBU's adoption of the foreign reserves neutrality principle, which should help contain inflationary pressure as highlighted in the buff statement. Could staff share their preliminary view on the impact of this approach? Nonetheless, inflation is likely to remain high given further liberalization of prices. We therefore welcome the authorities' plan to further tighten fiscal and monetary policy to reduce inflation as highlighted in the buff statement.

More importantly, we encourage the Uzbek authorities to reduce macroeconomic vulnerabilities arising from foreign currency exposures.

We commend the authorities for their commitment to fiscal prudence as reflected by low levels of public and publicly guaranteed debt. Nevertheless, we note with concern the substantial increase in Uzbekistan's public debt at end of 2017 due to exchange rate depreciation. In this regard, we invite staff to comment based on cross-country experiences how best the Uzbek authorities could manage such exchange rate risk. Further, we encourage the authorities to remain committed to increasing fiscal transparency as planned.

As the CBU is planning to move towards an inflation targeting framework over the medium-term, we underscore that the implementation of monetary policy should be supported by an effective monetary transmission mechanism. We agree that the CBU should strengthen its operational independence and capacity. In addition, we are of the view that a large amount of foreign currency used in the system limits the CBU's ability to implement monetary policy effectively. We therefore support staff's recommendation to reduce loan dollarization, which would help strengthen the transmission channel of monetary policy.

While the Uzbek banks are well capitalized and profitable, the financial system remains vulnerable to risks from credit concentration and currency mismatch. In this regard, we welcome the CBU's plan to incorporate stress testing in the supervisory process. We agree with staff's recommendation that banks should rely more on funding from households' deposits. To this end, we invite staff to share their view based on cross-country experiences on how to attract more deposits from households.

We welcome the authorities' New Development Strategy for 2017-21 towards building a more open and market-oriented economy. Successful implementation of the structural reform agenda hinges on strong political commitment.

We commend the authorities for significant progress made in improving the ease of doing business. Nevertheless, further efforts to improve the business environment will be crucial for sustainable and inclusive growth. As such, we note positively the authorities' acknowledgement of the need to restructure state enterprises and fight corruption. We also welcome the recent exchange rate unification and elimination of foreign exchange regulations inconsistent with Article VIII obligations. At the same time, we encourage the authorities to build on progress made to further liberalize prices and trade, and promote competition.

As pointed out in the report, Uzbekistan has a high share of working-age population that could potentially contribute as an important source of growth over the next two decades. Nevertheless, the current tax system disincentivizes firms to grow, hindering job creation and creating a heavy reliance on revenue collections from a small number of state enterprises. To this end, we are encouraged by the authorities' intention to put in place a comprehensive tax reform and agree that such reforms should be advanced gradually in line with improvements in tax administration capacity.

We take positive note of the authorities' strong efforts to improve statistics to increase data transparency as highlighted in the buff statement, which will be crucial for effective surveillance and policy making. In this connection, we welcome the Fund's provision of technical assistance to facilitate Uzbekistan's participation in the Fund's enhanced General Data Dissemination Standard.

On the EBA estimates, we are encouraged by staff's careful interpretation of model-based estimates to ensure that the assessments and policy recommendations have sufficiently considered recent developments of key variables and policies. We see merit in applying similar treatment to other individual countries' assessment given limitations of model-based estimates as explained in Annex I on the External Assessment, and ensure evenhandedness across the membership.

With these comments, we wish the Uzbek authorities success in their future endeavors.

Mr. Armas and Mr. Lischinsky submitted the following statement:

We thank staff for the set of papers and Ms. Barron and Mr. Kim for their illustrative buff statement. We commend the Uzbek authorities for the National Development Strategy (NDS) 2017-2021 and the five broad goals. This strategy introduces a wide-ranging reform agenda, aimed at opening and liberalizing a segmented economy to support the creation of more and better jobs, and diversify and increase the value-added in exports.

The high GDP growth (almost 8 percent in 2015 and 2016 an estimated 5.3 percent in 2017) does not push job creation, the average growth of employment in the period 2015-2017 (was 0.75 percent), which explains the measures to increase employment and take advantage of the opportunities that an increasing working-age population brings to the country. That said, could staff explain this low relationship between GDP growth rate in recent years and the growth rate of employment?

Inflation is high, around 20 percent in the first months of 2018, boosted by price and exchange rate liberalization, and the September 2017 depreciation. The authorities, following the staff's advice, intend to pursue tighter fiscal and monetary policy to control inflation. We note in Table 1 that the estimated GDP per capita (in U.S. dollars) has decreased sharply after depreciation. Is it possible to present the GDP per capita in real terms, that is, in PPP? The staff's comments are welcome.

The country relies on its large external buffers, international reserves of around 60 percent of GDP, and almost 20 months of imports at the end of 2017, to buttress the NDS, while the public-sector debt is low and sustainable, at 24 percent of GDP. The Uzbek authorities are willing to build a more open and market-oriented economy and, subsequently, transform the state-oriented economy. In this regard, what is the share of the public and private sector participation in the GDP? Growth is expected to be powered by private firms dependent on bank financing; what is the percentage of loans of public and private banks? How prepared is the private banking sector to deal with credit and capital requirements? The staff's responses are welcome.

Fiscal policy continued prudent and tax reform, as noted in the buff statement, is a top priority. Tax reform is needed, among others, to deal with SOEs and stimulate job creation beyond small enterprises. We concur with the authorities that tax reform should be based on the principle of revenue neutrality, projections should be realistic, and proceed gradually, while simultaneously improving tax implementation.

Monetary and exchange rate policies are supported by strong measures taken by the Central Bank of Uzbekistan, to lower inflation, raise the refinancing rate, and liberalize foreign exchange regulations. The central bank is assessing the appropriate monetary stance on several indicators, including interest and exchange rates. We commend the authorities for continuing to improve the monetary policy framework. Financial stability indicators are strong and the financial sector is profitable. NPLs are low, while loans are concentrated in state-owned enterprises. We welcome the authorities' commitment to create greater economic data transparency and their decision to join the General Data Dissemination Standard (GDDS).

With these comments, we wish Uzbekistan´s authorities and people all the best in their future endeavors.

Mr. Raghani, Mr. Bah and Mr. Bangrim Kibassim submitted the following statement:

We thank the staff for well-written reports and Ms. Barron and Mr. Kim for their informative buff statement.

The Uzbek authorities should be commended for initiating in 2017 a comprehensive reform program to address the daunting challenges facing the economy. In this regard, we are pleased to note the authorities' commitment under the National Development Strategy for 2017-21 to strengthen macroeconomic stability, achieve inclusive growth and improve the living standards of the population. The ongoing reforms have already led to the liberalization of many prices, the unification of exchange rates and the elimination of measures inconsistent with the country's Article VIII obligations.

Given that opening and liberalizing the economy has created new dynamic and constraints, we encourage the authorities to maintain the momentum of their reforms and continue implementing required measures to reduce inflation, strengthen fiscal policy and step up efforts to address structural bottlenecks to jobs creation, economy's competitiveness and business climate improvement. We broadly agree with staff's assessment and recommendations and will make the following comments for emphasis.

In the fiscal area, we encourage the authorities to pursue their prudent policy with a view to reduce deficits and increase transparency. The plan to reduce the fiscal deficit by cutting back on-lending activities is encouraging. Moreover, the authorities 'commitment to bring all fiscal operations on-budget beginning in 2019 is welcome. The envisaged measures to increase social safety net spending and improve the employability of the longer-term unemployed will be helpful in mitigating the impact of reforms on the vulnerable segment of population. We see merit in the authorities' tax reform as its implementation will ensure a fair system for small and large business entities, rationalize the VAT and further improve the tax administration that will help to create favorable conditions for an increased revenue collection. Given the capacity constraints attached to tax reform, we would appreciate The staff's comments on the Fund technical assistance to Uzbekistan to successfully achieve the objectives of this tax reform.

Regarding the monetary policy, the authorities have made good progress in improving their monetary and exchange rate policies. We note among other progress, the liberalization of foreign exchange regulations which has led the exchange rate to be determined by the market. We encourage them to further focus their efforts on containing inflation and further strengthening the central bank's institutional and operational frameworks. On the authorities' plan to adopt the inflation targeting, we agree that the central bank should improve its independence and communication strategy. In this regard, we see merit in the Fund providing a helpful technical assistance if needed. The staff's comments are welcome.

The Uzbek financial indicators appear strong and this performance should be maintained through the removal of the banking system vulnerabilities as the largest part of credit is concentrated in state enterprises. There is a need to continue preserving financial stability and promote soundness of banking system with the view of boosting economic growth. We welcome the authorities' reforms to upgrade the central bank's supervisory capacity and intervention tools.

On structural reforms, we take good note of progress made by the authorities and encourage them to further increase their efforts to promote competition and further liberalize trade and prices including energy prices. Moreover, we agree on the need to advance in the reforms of state enterprises to increase their operations and governance and reduce monopolistic practices while creating more room for the private sector development. It is also essential to increase the public's trust in the reforms and improve the country's investment climate with a view to attract the needed foreign investment.

Mr. Panek and Mr. Danenov submitted the following statement:

We thank staff for a comprehensive and very well-written report and Ms. Barron and Mr. Kim for their informative yet concise buff statement. We broadly concur with the thrust of the staff appraisal. We welcome the authorities' determination to liberalize the economy and conduct long-delayed reforms. Uzbekistan can benefit from the experience of other transition economies, including the neighboring countries. We encourage the authorities to continue improving their monetary and fiscal policies and taking resolute steps in implementing structural reforms. As staff state, sustained economic reform in Uzbekistan will be critical to the development of the region.

Tighter monetary policy is needed to contain inflation pressures as a result of price and foreign exchange liberalization. We acknowledge the apt conduct of monetary policy in the phase of liberalization, but concur with staff that CBU should now consider increasing the nominal refinancing rate. We welcome CBU’s new strategy based on foreign reserve neutrality, and encourage it to develop additional monetary policy instruments, such as open market operations. The recommended shift to inflation targeting over the medium term is welcomed. We caution, however, that the necessary conditions would need to be in place. These include a strong transmission mechanism and greater independence of the central bank, complemented by sound capacities and communication tools.

Liberalization of foreign exchange regulations should be implemented to their full extent. We welcome the abolishment of the long-lasting restrictions on foreign exchange and of the multiple currency practice. The staff assert in paragraph 13 that “current transactions” can be conducted “without impediment” In this regard, can staff confirm that all individuals and entities can freely buy foreign currency in cash, instead of receiving it on a special “conversion card” to be used only abroad?

Comprehensive tax reform is needed to boost entrepreneurship and improve the investment climate, while enabling adequate spending on education, health and public infrastructure. Simplification and unification of tax rates should replace the segmented and complex tax system that creates obstacles to job creation and constrains the growth of businesses. We concur with staff that reforms need to proceed gradually and in line with improvements in tax administration, and that the reforms should be based on the principle of revenue neutrality. Improvement of fiscal transparency and inclusion of the significant quasi-fiscal spending in the state budget in another imperative. Past fiscal prudence puts Uzbekistan in a good position to undertake these steps.

Addressing the many challenges faced by the banking system will be very important to further improve the growth outlook. State enterprises representing around 60 percent of the global loans portfolio are likely to see their profitability shrink. Bank’s asset quality could thus deteriorate. Looking further ahead, banks will need to become more efficient and raise funding and capital, while switching to more commercially-oriented business models. Opening up the financial system to foreign banking expertise would be beneficial.

We welcome the authorities’ decision to join the Fund’s enhanced General Data Dissemination Standard. We commend the intention to improve economic and financial statistics and to improve data transparency. This would considerably improve the basis for policy making. In this spirit, we encourage the authorities to consent to publication of the staff document.

Ms. Erbenova and Mr. Dogan submitted the following statement:

We thank staff for their report, and Ms. Barron and Mr. Kim for their candid buff statement. We broadly welcome the authorities' multi-pronged reform efforts aimed at further liberalizing the Uzbek economy, with a fundamental policy shift from a state-oriented economy to one that is more open, transparent, and market-based. Increased efforts to address institutional capacity weaknesses and benefiting from earlier transition experiences would ease the implementation and success of the reforms. As we agree with the thrust of the staff report, we will limit ourselves to the following comments.

While the Uzbek economy has had a robust growth performance, the low level of job creation remains of concern. Considering the relatively high share of the working-age population, the authorities should explore the ways to benefit from the opportunities presented by the available workforce and favorable economic environment. More rapid job creation should be one of the authorities' main priorities in ensuring inclusive growth. Considering the limited success of past policies in creating jobs, we would appreciate if staff could elaborate on the plans to generate adequate employment.

A more robust and upfront tax reform, addressing on-lending operations, as well as shifting to a more transparent fiscal framework are desirable to ensure a comprehensive fiscal consolidation. The tax reform appears urgent considering the complexity of the legislation; the number of exemptions; and the envisaged tax revenue decrease, should privileges for state enterprises be removed. Could staff elaborate on the preparations for the tax reform program and its expected impacts on the budget deficit? On the other hand, we welcome the low level of public debt. We support the authorities' efforts to gradually reduce on-lending operations to state enterprises to put the budget deficit on a sustainable path.

In addition to monetary tightening, modernizing the monetary policy and enhancing monetary instruments are needed to contain high inflation. Increased independence for the central bank, enhanced open market operations toolkit and a stronger transmission mechanism are necessary preconditions for an effective monetary policy to curb inflation and bolster price stability. We support the authorities' intention to move to inflation-targeting in the medium term. While we commend the Central Bank of Uzbekistan's considerable efforts, the authorities should stand ready to guard against the possible temporary impacts of the envisaged price liberalization and exchange rate fluctuations. We note the diverging views between the authorities and staff on the persistence of the recent inflation increase and near-term expectations, which seem to be rooted in different assumptions, especially at this time of ongoing deep, structural changes. We would appreciate staff's comments in this regard.

The liberalization of the foreign exchange rate market is an essential and welcome reform. Following an initial period of market adjustment to the removal of restrictions, the Uzbek economy should reap the benefits quickly. We believe that this reform will facilitate exchange rate flexibility as the first line of defense against external shocks. Removing restrictions will allow for further integration to the international trade system by eliminating unnecessary economic costs and supporting the flow of foreign direct investment into the country. Could staff elaborate on the liberalization's effects given the high loan dollarization?

The Uzbek economy is dealing with many structural reforms in the current transition period. We believe that reforms should, first and foremost, be well-sequenced, and the significant governance and capacity weaknesses have to be tackled in order to reach the goals in the welcome National Development Strategy for 2017-21. We commend the authorities' efforts to improve data transparency and, particularly, their decision to join the General Data Dissemination Standard.

Ms. White and Mr. Hemingway submitted the following statement:

We thank staff for a clear set of papers and Ms. Barron and Mr. Kim for their informative buff statement. We broadly share staff's assessment and welcome Uzbekistan's strong progress in initiating far-reaching reforms to put the country on track toward building a more open and market-oriented economy. We see completing and building on these reforms as key to tackling ongoing challenges in Uzbekistan, including those related to the large number of people entering the workforce each year.

We welcome the authorities' commitments to fighting corruption which we agree is a key priority for their development agenda. We note the staff finding that – for now – foreign investors remain on the sidelines, waiting to see whether reforms continue and prove durable. Ensuring proper tendering processes and transparency will be important in bringing these investors in. Absent these protections, we see a risk that FDI into Uzbekistan could happen on the basis of non-transparent and politically-motivated conditionality, with potential consequences for long-term stability. Do staff consider corruption to be a macro-critical issue for Uzbekistan? If so, we encourage them to provide analysis of its impact in the next Article IV.

Finally, we commend the positive impact of technical assistance on tax reform and improving statistics. We particularly welcome the Uzbekistan adopting of the IMF e-GDDS standard this year which we expect to increase quality and transparency of their statistics. We see government capacity to fully implement reforms as an important risk and one where the Fund can play a direct mitigation role through the provision of technical assistance.

Mr. Palei submitted the following statement:

We thank staff for the interesting report on Uzbekistan and Ms. Barron and Mr. Kim for highlighting the most important elements of the authorities' reform agenda. We welcome the recently intensified dialogue between staff and the Uzbek authorities, including technical assistance in the areas of tax reform, monetary policy, and statistics.

Like Mr. Fachada and Mr. Coronel, we are puzzled by the lack of Article IV consultations for almost three years. In 2015, at the time of the previous discussion we had raised similar concerns, as the previous lapse was also almost three years. Three years ago, staff intended to return to the normal 12-month surveillance cycle, but it did not happen. We ask staff to explain the reasons for the repeated major deviations from the established Fund policies.

We also note that the report is again very brief and it is not accompanied by a selected issues paper. Given the recognition of the magnitude of possible changes in Uzbekistan's policies, the absence of supporting research is especially regrettable. We would appreciate staff's explanation on the reasons for their choice of format for the Article IV report and on whether any research is planned on this large economy facing complex policy challenges and undergoing systemic reforms.

Another point also made by Mr. Fachada and Mr. Coronel was about the high real GDP growth rates in Uzbekistan. We believe that during the period since 1995 used by staff in Figure 1, the average annual growth of the Uzbek real GDP per capita was almost 5 percent. The staff may want to confirm this number. More clarity would be useful to better understand staff's arguments about the pace of reforms envisaged by the authorities.

We agree with staff that the Uzbek economy has enviable starting conditions. There is some growth slowdown, but it seems to be less pronounced than in most other countries in the region and globally. To some extent the slowdown could be explained by the delay in foreign exchange rate adjustment. After the depreciation, unification of the exchange rates and the authorities' move to a more flexible arrangement, there was a spike in inflation. The pressures on prices are dissipating, though, and staff agreed that the authorities' overall response was appropriate. At the same time, foreign exchange reserves are still very large. Public debt is low, although vigilance is necessary for preserving prudent fiscal policy going forward. High growth rates, healthy public balance sheet, favorable demographic situation, and engagement with a range of development partners bode well for economic success.

We broadly endorse the authorities' reform agenda for the medium-term and also agree with the priorities emphasized by staff in their report. We agree that more attention to fiscal transparency, maybe with the assistance of the Fund, would be essential to ensure budget accountability and also to strengthen the institutional framework for maintaining public investments at a level conducive to maintaining high growth rates. Did staff discuss with the authorities an evaluation of fiscal transparency report as a stock-taking exercise? What are the key areas of fiscal transparency the authorities have to focus on?

In the monetary area, we welcome the dialogue on a gradual transition to an inflation targeting framework. Given the experience of other countries in the region, at this stage, it would be important for the authorities to avoid dangerous dollarization of the economy.

On the external sector, we agree with the authorities' views on the pitfalls of relying on the estimates produces by the EBA lite applications. The authorities would be well advised to preserve external stability instead of allowing large current account deficits in the medium term. Given the role of remittances for the balance of payments, we would be interested in the estimates of these flows since the middle of the 2000s, and not just in the U.S. dollar terms, but also as a percentage of GDP. We note that staff project steady and significant rise in the number of labor migrants from Uzbekistan from about 1 million in 2015 to about 1.5 million in 2019. While we understand that the numbers may not be very precise, the scale of changes poses important questions about future developments in the external sector and labor market in Uzbekistan.

Finally, we agree with staff that, despite the evident progress in some structural reforms over the past years, there is significant room for additional improvements. We hope that staff can continue to assist the authorities in identifying policy priorities and implementing reforms. We look forward to a more detailed consideration of the important reform agenda, as well as of policy implications related to demographics in Uzbekistan in the future working papers, SIPs, and Article IV reports.

Mr. Mojarrad and Mr. Badsi submitted the following statement:

We thank staff for the well-written papers and Ms. Barron and Mr. Kim for their informative buff statement.

The Uzbekistan economy has recently embarked on a comprehensive reform process, to open and liberalize the economy. We welcome the authorities' commitment to ensuring macroeconomic stability while achieving inclusive growth. Although still relatively robust, economic growth slowed in 2017, but is projected to strengthen in the medium term. Against a backdrop of elevated unemployment rate, price and exchange rate liberalization have led to higher inflation, the augmented fiscal deficit widened, but the external position strengthened. With low risk of external debt distress, risks to the outlook are skewed to the downside, mainly stemming from lower commodity prices and domestic risks, including from spillover of reforms on the financial sector. We are in broad agreement with the staff appraisal.

We welcome the authorities' commitment to prudent fiscal policy and to bringing all fiscal operations on the budget. Although increasing in 2017, and thanks to better control on spending, the fiscal deficit is expected to decrease this year to a more sustainable level. With high inflation pressures, the fiscal policy needs to be tightened while improving budget transparency. We take positive note of the authorities' recognition of the need for a larger fiscal adjustment over the near term, and encourage them to broaden the tax base and strengthen tax administration, including by addressing the tax regime segmentation. We commend the authorities for their recent efforts to reform the customs and pension systems, as indicated by Ms. Barron and Mr. Kim.

Financial sector indicators suggest that the banking sector is healthy, with adequate capitalization, high profitability, and low level of NPLs. However, like most other economies in transition, the credit market is still segmented, with significant preferential government lending to state enterprises. We call on the authorities to preserve financial stability and guard against spillover of price liberalization and other reforms on the profitability of state enterprises, which could adversely impact banks' asset quality. The monetary tightening initiated in the second half of 2017, prior to FX liberalization, is appropriate, but a stronger stance of monetary policy and a more efficient monetary transmission channel are needed in view of the high inflation.

We encourage the authorities to strengthen their efforts toward laying the foundations for higher, more sustainable and inclusive growth, including by improving competitiveness, state enterprise restructuring, and greater trade liberalization. We look forward to tangible progress in improving the investment climate. We commend the authorities for their efforts in promoting diversification and increasing value-added in exports, and are comforted by the implementation of the recent measures aimed at improving the quality and availability of economic data. We support Mr. Fachada and Mr. Coronel's views on the need for adequate sequencing and prioritization of the reform agenda to avoid political or capacity setbacks.

We wish the Uzbek authorities success in their future endeavors.

Mr. Jang informed the Board that the Uzbek authorities had consented to publication of the staff report.

Mr. Mkwezalamba made the following statement:

We thank the staff for the concise report and Ms. Barron and Mr. Kim for their informative buff statement. We did not issue a gray statement but would like to acknowledge the Uzbek authorities' continued efforts to implement their reform agenda, including putting data on a sustainable path, improving monetary and exchange rate policies, and strengthening the external position. We broadly agree with the staff's assessment and recommendations and wish to make the following comments for emphasis.

First, at the current level of about 20 percent, inflation is quite high. Moreover, medium-term structural reforms are likely to include price liberalization and cost recovery pricing adjustments for the energy sector, both of which will put further upward pressure on prices. For these reasons, we join other Directors in calling for tighter monetary policy as a means of anchoring inflation.

Second, while capital account liberalization is key, it is not clear from the report what type of capital flow management measures (CFMs) are in place and how the reform will be sequenced. Given Uzbekistan's investment push and strong external position, higher capital inflows may be likely over the medium term, which would also help with inflation as the currency appreciates. We would appreciate comments by the staff.

Third, we commend the authorities' commitment to structural reforms, including implementing tax reforms, as outlined by Ms. Barron and Mr. Kim in their buff statement. This is being done with a view to increase competitiveness, improve the business environment, and develop the needed infrastructure to support rapid job creation. While the reform agenda is justified, we also welcome the staff's comments on measures put in place to protect vulnerable groups against the unintended consequences of the reform measures.

Fourth, while financial soundness indicators are strong, loan concentration in state-owned enterprises (SOEs) presents challenges, and asset quality could deteriorate if external shocks materialize. However, we are comforted that the upcoming report of the consulting group on SOE governance will contain recommendations to address the legacy issues of SOEs. That being said, it will be critical that recommendations are implemented in a timely fashion.

Finally, we associate ourselves with Mr. Fachada's and Mr. Coronel's comment that transitioning to a market-oriented growth model is both a challenge and an opportunity for Uzbekistan. But since other countries have followed this path before, we urge the authorities to draw from the lessons identified in Box 2 since they contain important principles for success.

Mr. Panek made the following statement:

We welcome the recent opening of Uzbekistan and the initiation of a reform program. Uzbekistan can play even a bigger role in regional affairs, and its cooperation with neighboring countries is important for the prosperity and stability of the region. We agree that Uzbekistan has a good starting position to initiate the wide-ranging reform program, and the beginnings of this program seem optimistic. However, Box 2 of the staff report entitled "Seven Lessons from Earlier Transitions" deserves a careful reading.

The road ahead may become bumpy and full of challenges. I will mention two that can be decisive. The first is related to SOEs fighting back when their vested interests are violated. But the challenge related to the labor market will probably be the most important one. Reforms increase expectations that can derail the reform program if they are not met. Uzbekistan must create many jobs to meet the demand of its working-age population. Good jobs will improve living standards. If job creation is too slow, many new migrants will leave the country; and it is usually the better-educated, more open-minded, and active people that leave first, depleting the country of the human capital that is essential for reforms to succeed.

We know that the private sector is more efficient in creating jobs, so its development is decisive for the future of the labor market and the future of reforms.

Mr. Castets made the following statement:

I thank the staff for the set of papers and the answers to our written questions. I also thank Ms. Barron and Mr. Kim for their helpful buff statement.

We are pleased to have this discussion after almost three years without an Article IV review for Uzbekistan, especially given the significant changes that the Uzbek economy has experienced over the past few months. We are particularly pleased to hear the authorities' commitment to publish the Article IV report. It is a good signal.

We commend the authorities for the impressive set of reforms that have been implemented in a short period of time. These are steps in the right direction toward an open and market-driven economy, and the liberalization of the foreign exchange regulations last September is a significant change.

I would like to address one issue that we did not cover in our gray statement—external sector assessment—because reading the gray statements, we thought that there was some questioning among Directors. For our part, we thank the staff for a nuanced and clear presentation of the external sector assessment in the context of uncertainty about the data. Beyond the description of the figures, the important message to the authorities is that the current account deficit would not be abnormal for a developing economy like Uzbekistan.

We note that the results obtained through the External Balance Assessment (EBA) approach must be further analyzed in light of the recent changes, but we still believe that the EBA gives useful guidance on a given economic situation, including for Uzbekistan.

Mr. Palei made the following statement:

I thank the staff for a good report and also for the written answers to Directors' questions. I am also glad that the authorities decided to publish this report. It is a welcome step that will probably contribute to the policy discussions that are ongoing. In the beginning of this report, there is this notion that Uzbekistan's economic results are mixed. It is not clear whether they are positive or not. But when one looks at the numbers for real GDP growth, they look amazing. The staff noted that the per capita real GDP growth was 6.5 percent for more than 20 years. This result is on par with the highest growth rates in the world—such as India today or even close to those of China for a sustained period of time. The results are very good. This notion that there is a need for drastic changes and a break with the old model should be moderated. The country is in a good position in terms of the public balance sheet. Their government debt is low. Fiscal deficits are low. Foreign exchange reserves are very high. The estimated share of the state-controlled economy provided by staff is about 25 to 30 percent, which is not very high. It is common in many countries, including more developed countries.

Uzbekistan is in a good position. It has relatively high income. If we look at GDP per capita in purchasing power parity (PPP) terms, the staff noted that it may be underestimated by about 20 percent because the gray market or black-market economy, the informal economy, is not calculated. It could be close to the level of The Philippines, Laos, Armenia, or similar countries.

The country is in relatively good shape in terms of initial transitions. We are pleased that the authorities intensified the dialogue with the Fund, that a significant amount of technical assistance is provided. We encourage the staff and the authorities to continue on this path. In particular, we noticed that there is an agreement to conduct a fiscal transparency evaluation. The staff said that we will hear about it next time. I am not sure whether we will have it in 12 months or in two or three years; but hopefully the staff can tell us at least the basics about the key areas of subsidies, SOEs, or off-budgetary funds. I look forward to the additional answers the staff promised us in the written responses.

The staff representative from the Middle East and Central Asia Department (Mr. Jaeger), in response to questions and comments from Executive Directors, made the following statement:[1]

There were a number of questions in the gray statements. We counted 48 questions. In a way we are glad that we did not have selected issues papers because otherwise the number of questions might have reached record

[1] Prior to the Board meeting, SEC circulated the staff's additional responses by email. For information, these are included in an annex to these minutes.

territory. We hope that the team's responses were useful, but we are happy to follow up on some of the responses if desired.

I want to start by giving a bit more information on the reasons for the delay of the Article IV consultation. Then I would like to address the questions on the proper policy mix, especially the role of fiscal policy in the mix, and then I would like to touch on the challenge of tax reform.

On the delay of the Article IV consultation, it is helpful to be aware of some of the background because this is also relevant for some of the technical questions on GDP growth and inflation. Before the change of course in the middle of last year, two issues created special difficulties in our Article IV consultation process with the authorities. The first issue was the foreign exchange market and exchange restrictions. Some of them, in the staff's view, were running counter to the Article VIII obligations. The authorities did not agree with our assessment of the foreign exchange market restrictions, and they also argued that the foreign exchange black market is illegal and also small and unimportant.

The second difficult issue we faced was the quality of statistics. The staff felt that to some extent the GDP growth numbers and the inflation numbers were based on wishful thinking. We were obliged to bring up these issues with the authorities. Our counterparts felt obliged to deny that there were significant problems. This was not an ideal setting for a smooth Article IV process. Toward the end of 2016 when the Article IV consultation was already overdue, there was a change in government, and this further delayed the Article IV process. At that point it was not clear which policy directions the new government would take, but by June 2017, the authorities had decided where to go. They immediately contacted us at that point and wanted close cooperation on their reform agenda, especially the liberalization of the foreign exchange market.

There were further delays in the Article IV consultation since mid-2017. One reason was that we had to assemble a team. Meanwhile, the authorities wanted first to focus on the foreign exchange market liberalization, and they also wanted help in designing a new macroeconomic framework that was needed because they were engaging with other international financial institutions, especially the World Bank and the Asian Development Bank.

With the benefit of hindsight, we feel somewhat vindicated regarding our views on the foreign exchange market situation and the statistics. On the foreign exchange market, the authorities' new economic team immediately agreed that about half of all foreign exchange transactions were going through the black market. This was a comforting fact, given that they were planning to unify the official exchange rate with the black-market exchange rate; and the expectation was there would be a significant depreciation in the official exchange rate.

On the statistics issue, the best I can do is to quote the president himself from a recent speech he gave to parliament and the diplomatic corps. The president said, “We have ended our wishful thinking, and this is one of the main changes in our economic policy. If in previous years we talked about 8 percent GDP growth, now it is only 5.5 percent, but the information is now actual and proven.”

In fact, it is difficult to overestimate this change in how the authorities approach the quality and availability of statistics. Just yesterday, the authorities started to publish a wide range of macroeconomic and financial indicators on their national summary data page. Within half a year, we have gone from a situation where many economic and financial statistics were considered classified information, which was not even shared with the World Bank, to a situation where all these data are in the public domain.

Against this backdrop and the presently close cooperation that we have with the authorities, we can be reasonably confident that the consultation cycle will become much more regular in the future.

Now let me turn to the question of the appropriate policy mix. The report advocates, and the authorities agree, that there is a need to tighten monetary and fiscal policy. By fiscal policy we mean the overall fiscal stance, including on lending operations to SOEs.

Before I go to the policy mix, I have a clarification on the growth forecast. The buff statement notes that the authorities project 6 percent growth in 2018 and 2019, while the staff projects 5 percent. The authorities, in fact, have a range forecast for GDP growth. For 2018, they have a range between 5.5 percent and close to 6 percent. They do not have a forecast for 2019. They do not forecast two years ahead. The difference between our growth forecast is a bit smaller than it may appear at first.

The main question on the policy mix seems to be why do we not use expansionary fiscal policy to reverse the slowdown in GDP growth from the traditional 8 percent while using monetary policy to fight inflation? The first answer is that the 8 percent GDP growth is unlikely to be the growth rate of potential GDP at this point. This goes back to the quote by the president, but if one looks at indicators like inflation and the current account, we do not feel there is a lot of slack in output accumulating. Inflationary pressures are high. We see the current account shifting rapidly from surplus to deficit.

Given that evidence, we believe it is justified that fiscal policy, including on-lending operations, will be tightened. Where it is important to note the difference is between the fiscal stance that includes the on-lending operations and excludes on-lending operations. As was noted in some of the gray statements, once we take out the on-lending operations, we have a slightly expansionary fiscal stance.

Turning to the tax reform issue, this is the next big reform, and it is a very important reform. There is agreement that the present tax system in Uzbekistan is very distortive. It is a break on job creation, and there is an urgent need for reform, so there is full agreement on all sides on that. There is also agreement on where the tax reform should end up. On the indirect tax side, the aim is to have a modern value-added tax and excise tax system. On the corporate income tax side, there should be a level playing field across all companies, whether state-owned or private. As regards personal income taxation and social contributions, there is a need to reduce the overall burden on labor.

There is full agreement on the end point of the tax reform. The question is how do we get from here to the end point? There is one view that the shift should be as quick as possible. However, in our view—and this goes to our assessment of the readiness of the tax administration and also the readiness of the taxpayers to facilitate the shift to a very different tax system—we believe that the more gradual approach should be taken. In addition, if there are large revenue shortfalls caused by the tax reforms, we are concerned that this could affect the stability orientation of the fiscal policy.

Mr. Jang made the following concluding statement:

It is my pleasure to speak on behalf of Uzbekistan in my first Board meeting as Executive Director. I would like to thank the mission team for their thorough assessment and constructive discussions, and I also want to express my appreciation to Directors for sharing useful comments in their gray statements and in today's meeting.

There is a Korean saying: A journey of a thousand miles must begin with a first step. Last year, the new Uzbek government began wide-ranging reforms with an important first step. This was to unify the official and parallel market foreign exchange. Other reforms have followed, including price liberalization, SOE reform, more central bank independence, and an improvement in statistics.

Alongside these courageous reforms, economic growth has remained robust at more than 5 percent. Inflation has been high due to price liberalization and the depreciation of the currency. The authorities intend to conduct tight fiscal and monetary policy to help contain this.

As Mr. Gokarn, Mr. Armas, and Ms. Erbenova mentioned in their gray statements, the Uzbek authorities face the issue of low job growth; but we are confident that the structural reforms and improvement to the business environment will begin to arrest this. Also, as Mr. Doornbosch indicated, the authorities are implementing market programs that will work to absorb the strong increase in the working-age population. I also agree with Ms. Pollard that the authorities should maintain their positive momentum and press ahead with their reforms to create more job opportunities.

Finally, I would like to comment on the delay in the Article IV consultation. Last year there was a political sea change in Uzbekistan following the death of the first Uzbek president. The new president was elected, and a new economic team was appointed; and the country began to embark on its reforms. These circumstances should be fully considered.

The Acting Chair (Mr. Zhang) noted that the Republic of Uzbekistan is an Article VIII member, and no decision was proposed.

The following summing up was issued:

Executive Directors agreed with the thrust of the staff appraisal. They welcomed that Uzbekistan has initiated a comprehensive reform program to open and liberalize the economy, stimulate job creation, and promote inclusive growth. Noting the internal and external risks to the outlook, Directors encouraged the authorities to maintain prudent macroeconomic policies and the momentum of structural reforms. In this regard, they underscored the need for tighter fiscal and monetary policies to gradually bring inflation to single digits.

Directors commended the authorities for their prudent fiscal policies, which have kept public debt low. They supported the plans to reduce the overall fiscal deficit in 2018, mainly by reducing on-lending operations by the

Fund for Reconstruction and Development. Directors emphasized the importance of ensuring that all fiscal operations are brought on budget. They also underscored that a comprehensive reform of the tax system is essential to foster job creation and to insure against the risk of a sharp future decline of tax collections from state enterprises. They advised that reform should be introduced gradually and should be revenue neutral to preserve a stability-oriented fiscal policy.

Directors agreed that the central bank should use a range of indicators, including the refinancing rate, bank liquidity, money, and the exchange rate, to gauge the appropriate stance of monetary policy. They noted that it will be important to enhance the independence of the central bank to support the adoption of inflation-targeting over the medium term.

Directors noted that reported financial sector indicators are strong, but the concentration of credit in state enterprises is a vulnerability. They welcomed plans to further upgrade the central bank's supervisory capacity and intervention tools. Directors underlined the importance of policies fostering a banking system that is inclusive and supports growth over the medium term.

Directors commended liberalization of the foreign exchange market, including the elimination of exchange restrictions. They noted that while Uzbekistan's external position is strong, it could be impacted by changes arising from the economic transition and Uzbekistan's dependence on remittances and commodity exports. Directors welcomed the authorities' intention to allow the exchange rate to adjust in line with fundamentals to help safeguard external stability and maintain scope for an independent monetary policy.

Directors welcomed the significant structural reforms underway. They emphasized that priorities ahead should focus on restructuring state enterprises and further trade and price liberalization, especially by raising energy prices to cost-recovery levels, and promoting competition. Directors also welcomed the recent governance reforms and encouraged continued efforts to fight corruption and enhance the rule of law. They underscored that economic diversification, especially into sectors with higher human capital content would support the country's fast-paced demographic transition.

Directors commended recent steps to improve the availability and quality of economic statistics and welcomed Uzbekistan's participating in the IMF's enhanced General Data Dissemination System (e-GDDS). They looked forward to further improvements towards subscribing to the Special Data Dissemination Standard (SDDS) as part of their participation in the e-GDDS.

It is expected that the next Article IV consultation with the Republic of Uzbekistan will be held on the standard 12-month cycle.

APPROVAL: April 20, 2020

JIANHAI LIN
Secretary

Annex

The staff circulated the following written answers, in response to technical and factual questions from Executive Directors, prior to the Executive Board meeting:

Recent Developments, Outlook and Risks

1. Since both the projections assume that growth will be supported by strong commodity prices and trading partner demand, reforms that boost agriculture, and the government's housing and infrastructure programs, why is there a difference in the final projected rate [for growth and inflation]?

2. Can staff comment on the diverging views between the authorities and staff on the persistence of the recent inflation increase and near-term expectations, which seem to be rooted in different assumptions, especially at this time of ongoing deep, structural changes?

(Response to previous two questions)

- The difference in inflation projections between staff and the authorities reflects differences in the assumptions regarding the persistence of inflation and the pass-through of the exchange rate depreciation to inflation.

3. Given that the authorities plan to tighten both monetary and fiscal policy in 2018 to reduce inflation, what other measures can the staff propose to bring down the rate of inflation, whose persistence could be detrimental to the economy by choking off economic activity?

- As part of the structural policy agenda, increasing competition in the domestic market for goods and services could be an important contribution to lower persistence of inflation, especially if the nominal exchange is taking on a bigger role as a stabilization tool. Maintaining a moderate stance on incomes policy in the public sector, as foreseen in the fiscal projections, will also be important.

4. Could staff comment on factors contributing to the substantially lower medium-term growth projections compared to the 2015 Article IV consultation?

- The 2015 Article IV projections were predicated on a continuation of the previous growth model and did not take into account more recent data. For example, the previous projections expect a continuation of the authorities targeting of small fiscal and external surpluses and fiscal dominance the resulted in higher inflation.

- The 2018 Article IV projections expect somewhat higher fiscal and external deficits that result from greater investment as reforms take hold. On growth, revisions to the authorities estimates resulted in lower growth estimates for 2017. The staff expects future estimate will be more in line with these lower estimates. Over the medium term, growth should pick up as reforms and higher investment have an impact.

5. What is the share of the public and private sector participation in the GDP?

- The best available estimate of the share of state enterprises in GDP is about 25 percent. In addition, budgetary organizations included in general government contribute about 10 percent to GDP, mostly through the public wage bill. Thus, the share of the public sector as whole in GDP would be about 35 percent.

- Official estimates of the share of the public sector in GDP are closer to 20 percent, but these estimates include only enterprises that are 100 percent owned by the state.

Fiscal Policy and Debt Sustainability

6. What are the staff' views on the recommended policy mix balance between budgetary support and tighter monetary policy and on the most effective budgetary channels?

- Questions on policy mix and overall fiscal and monetary policy to be answered orally.

7. The fiscal deficit increased from 0.6 in 2016 to 3.3 in 2017, mostly attributed to the amount of loans extended by the FRD to state enterprises (SEs) and for state banks' recapitalization; by the same means, the bulk of the fiscal adjustment in 2018 would mainly come from a cut in FRD lending operations. Can staff clarify why these loans are treated as expenditures and if the authorities have adopted a broader policy to limit the amount of FRD loans to SEs?

- The guidance on the treatment of net lending in government financial statistics as varied over the years. If government lending is used provided credit at preferential rates, it is also akin to a government subsidy and therefore treated as an expenditure items.

- In terms of limits, the authorities are targeting a zero balance for the FRD. The staff has encouraged the authorities to bring FRD operations on budget and to reduce on-lending.

8. We also would like to understand better the budget classification of expenditures presented in Tables 4 and 5, in particular, which of those are mainly wages?

- Under government budget, the expenditures with the largest wage component are social and cultural expenditures and the social safety net.

9. What implications would this medium-term increase in fiscal deficit and public debt have for the fiscal space and overall macroeconomic balance in the economy?

- The increase in the public debt ratio from 10½ to 24½ percent of GDP from 2016 to 2017 primarily reflects the impact of exchange rate depreciation. Even at the higher level, all of Uzbekistan's debt indicators are well below standard benchmarks (see DSA).

- As the effects of tax and state enterprise reform entail risks and there is little evidence that GDP growth is underperforming potential, there is not a case at present for fiscal stimulus and fiscal space can be used to insure against risks arising from reforms.

10. Could staff elaborate on the preparations for the tax reform program and its expected impacts on the budget deficit?

- A first preliminary proposal for reforming the tax system was published in early April. This proposal envisages shifting to a tax system that is closely modelled on Georgia's status quo tax system.

- If implemented immediately, i.e. at the beginning of 2019, it would entail large revenue losses when costed at the tax rates spelled out in the proposal. This proposal is now under discussion, both as regards the pace of implementation as well as the substance of the reforms of the corporate tax on the one hand and the personal income tax and social contributions on the other hand.

- The authorities have requested additional technical assistance on tax policy and tax administration from the Fund to study the options.

11. Did staff discuss with the authorities an evaluation of fiscal transparency report as a stock-taking exercise?

- The authorities have requested an assessment of fiscal transparency; FAD is likely to field a mission in June.

12. What are the key areas of fiscal transparency the authorities have to focus on?

- The already scheduled fiscal transparency assessment will provide answers to this question.

13. Can staff comment based on cross-country experiences how best the Uzbek authorities could manage such exchange rate risk [increase in public debt due to exchange rate depreciation]?

14. Can staff comment whether the reported lack of data and the application of the new DSA framework could impact the risk assessment?

(Response to two previous questions)

- In general, countries face a trade-off regarding local currency vs foreign currency debt. Local currency debt avoids external risks, but is usually carries a higher interest rates, concentrated in shorter maturities, and can potentially crowd out of other domestic borrowers.

- The right balance of local and foreign currency debt depends on the type and duration of external shocks a country faces, the demand curve for their debt by non-residents, and the state of capital market development.

- In Uzbekistan, domestic debt was fully retired in 2016 and the local bond market is underdeveloped. The staff supports the authorities' plan to consider restarting issues of treasury bonds.

- As noted in the DSA, public external debt is currently sustainable. The public debt to GDP ratio is relatively low at 24½ percent of GDP, even after the devaluation, while gross international reserves of the central bank are around 60 percent of GDP.

- The new DSA framework will enhance the risk analysis by adding new tools to assess the realism of macro assumptions, more focus on country specific fundamentals, broaden the classification used to assets debt carrying capacity, and simplify debt indicators and thresholds.

Given that Uzbekistan is well below standard debt thresholds, staff expects this will enhance the analysis but not affect the baseline assessment.

Monetary and Exchange Rates

15. Which additional measures could be taken to improve the de facto independence of the central bank?

16. Can staff comment how central bank independence has evolved de jure and de facto in the course of reforms?

(Response to previous two questions)

- Until recently, the CBU was nominally independent, but in practice implemented its policies in line with instructions provided by the Cabinet of Ministers. A recent decree formally abolished this practice.

- We do not have available a formal coding of the traditional components of indices of central bank independence, such as terms of appointment and dismissal of central bank management, central bank's role in policy formulation, objectives of the central bank, and limitations on central bank lending. Our sense is the formal score would presently point to relatively low independence.

- The drafting of a new law on the central bank is underway, and the authorities have requested staff's input to make sure that the new law reflects best international practices, also in view of the plan to adopt inflation targeting over the medium term.

17. The Central Bank of Uzbekistan (CBU) did tighten its monetary policy in preparation of the exchange rate liberalization but has since maintained stable nominal exchange and refinancing rates. Can staff comment on the reasons behind this policy choice and the weakness of monetary policy transmission channels in Uzbekistan?

- The CBU has indicated that it does target the exchange rate. Nonetheless, the exchange rate has stayed within very narrow (±1 percent) bands since unification in September 2017.

- On transmission channels, econometric estimates have not given strong estimates of the relationship between inflation and plausible exogenous factors (e.g. the money supply, interest rates, or the exchange rate). Moreover, with the substantive structural changes in pricing and lifting of restrictions on access to foreign exchange, it is expected that previous relationships would be changing.

- Thus, the transmission channel is particularly uncertain at this stage and staff has recommended that the authorities use a number of different indicators to judge the stance and impact of monetary policy.

18. We see some differences between staff's policy advice and the strategy being pursued by the authorities…while staff recommends an additional increase in the nominal refinancing rate and halting FX accumulation by introducing a regular pre-announced program of FX sales from the CBU's gold purchases, the authorities consider that the current level of the refinancing rate is appropriate and have adopted a neutrality principle which means gold purchases and sales would be

equal. Can staff clarify this apparent difference in criteria and therefore how the CBU intends to tighten MP?

- The differences in views on the refinancing rate mostly reflect different views on the persistence of inflation. The authorities' inflation outlook is more optimistic, and they therefore see much less need to increase the nominal refinancing rate to bring the real rate back to positive levels.

- There is no real difference on FX accumulation policy. Halting FX accumulation on the one hand and adopting a neutrality principle on the other hand are in substance equivalent policies as the accumulation of FX reserves is largely effected through purchases of gold.

19. Can staff also indicate which operational tools does the CBU have currently available and what the specific TA recommendations are to strengthen the existing toolkit?

- The CBU has a number of operational tools. These include: (i) 3 standing facilities of which the primary one is the refinancing window that provides liquidity to banks and (iii) reserve requirements of 10-15 percent on banks' domestic and foreign currency liabilities. The CBU does not conduct open market operations.

- To strengthen monetary operations, staff is recommending: (i) consolidation of standing facilities into an overnight or one-week facility; (ii) introduction of a standing overnight deposit facility; and (iii) the introduction of open market operations and consideration of issuance of government securities.

20. We note positively the CBU's adoption of the foreign reserves neutrality principle, which should help contain inflationary pressure as highlighted in the buff statement. Could staff share their preliminary view on the impact of this approach?

- The neutrality principle along with a steady nominal exchange rate has resulted in a substantial tightening of monetary policy (see text table). Prior to the depreciation of the official exchange rate in September 2017, net foreign assets of the CBU (measured in domestic currency) rose at an annualized rate of 60 percent, contributing to an annualized growth rate of 89 percent in reserve money and 30 percent in broad money.

- Following depreciation, growth of net foreign assets of the CBU, reserve money, and broad money slowed to 5, 14, and 1 percent, respectively, on an annualized basis.

Uzbekistan: Reserves, Exchange Rate, and Monetary Aggregates						
	Dec 2016	Aug 2017	Annualized Change	Sep 2017	Mar 2018	Annualized Change
Monetary Authorities						
Gross international reserves (USD billions)	26.5	27.8	7%	28	28.5	4%
Net Foreign Assets (Som billions)	84,531	115,647	60%	223,198	228,327	5%
Reserve Money (Som billions)	17,274	26,375	89%	29,822	31,859	14%
Monetary Survey						
Net Foreign Assets (Som billions)	92,705	128,031	62%	246,665	251,329	4%
Broad Money (Som billions)	52,041	62,002	30%	73,443	73,854	1%
Nominal Exchange Rate (UZS/USD)	3,231	4,210	49%	8,078	8,115	1%
Refinancing Rate (percent)	9.0	14.0	94%	14.0	14.0	0%
Consumer Price Index (level)	260	282	13%	286	324	28%

21. The report is silent on the social impact of such a depreciation of the exchange rate on the population, notably the most vulnerable, and the adequacy of the strengthening of the social safety nets. Can staff comment?

22. We wonder if in the case of Uzbekistan, it could be useful to acknowledge proper policies to mitigate potential negative effects [from increasing of the exchange flexibility constitutes] in future policy advice. Can staff comment?

(Response to previous two questions.)

- Depreciation of the exchange rate may have an impact on the poor, although the extent of the impact is unclear. It is expected that the prices of imported products will rise thereby lowering consumers real incomes.

- However, individuals and private firms were previously excluded from using the official rate and already used the black-market exchange rate. Thus, the impact on purchasing power may be less than indicated by the depreciation of the official exchange rate.

- As indicated in the staff report and the buff statement, the authorities intend to focus the budget on mitigating the impact of the exchange rate on the vulnerable. Indeed, the increase in expenditures as a percent of GDP in 2018 is almost entirely due to the one percent of GDP increase in expenditures on the social safety net.

External Sector

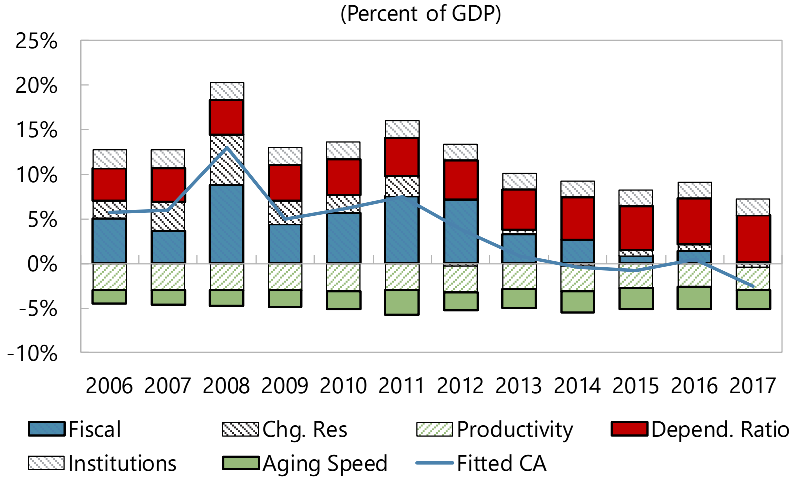
23. We agree with the staff's appraisal that the large depreciation in September 2017 suggests that the external position was not as strong as suggested by the EBA model. We would appreciate further information on the factors leading to the change in the current account norm estimated by staff.

- The staff made no adjustments to the EBA-Lite model, which resulted in a current account norm of – 2¼ (±1) percent of GDP, which appears reasonable for a developing country with Uzbekistan's characteristics. With a preliminary estimate for the 2017 current account balance of +3¾ percent of GDP, this results in a gap estimate of +6 (±1) percent of GDP.

- There are several factors which are not taken into account in the EBA-Lite model. First, the 2017 current account balance is preliminary and larger than in previous years and so may be an outlier. Second, the model is backward looking and does not take into account more recent developments. In particular, trade data for the first quarter show a rapid rise in both exports and imports which make forecasting the current account in 2018 particularly uncertain. Third, while the exchange rate depreciation would be expected to raise the trade balance going forward, the model does not take into account the lifting of restrictions on access to foreign exchange and the reduction in import tariffs. It is not clear at this stage which will have the bigger impact.

- The main factor contributing to changes in the estimated current account norm is the fiscal balance. Including net lending operations, Uzbekistan's fiscal balance declined from a peak of almost 8 percent of GDP in 2012 to a deficit of 3¼ percent of GDP in 2017. With a weight of 0.53 in the model, this reduced the current account norm by 6 percent of GDP over the same period.

Uzbekistan: Current Account Norm Contributions
(Percent of GDP)

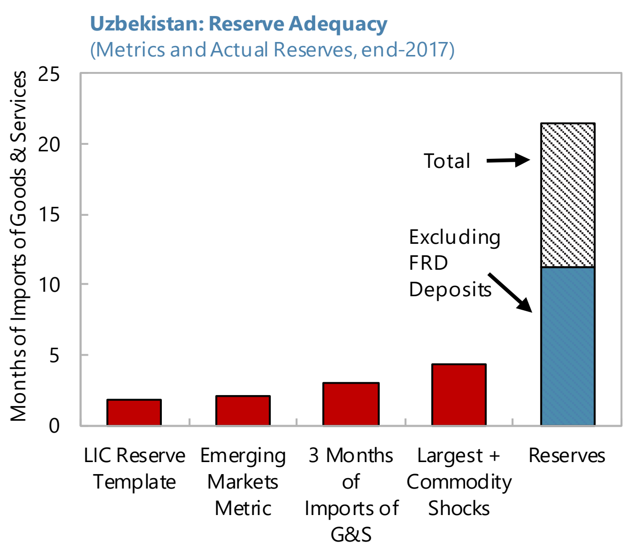


24. We note that assets of the FRD are included in the reserve metric but are not considered available to insure against external shocks or for central bank FX operations. Could staff elaborate on why these assets are included in the reserve metric anyhow?

- BPM6 notes that (i) reserves are external assets readily available to and controlled by the monetary authorities, (ii) does not exclude assets that are committed for future use, and (iii) there is a presumption that external assets of special purpose government funds on the books of the central bank are reserve assets (see excerpts below).

- On this basis, assets of the FRD are included in the reserve metric.

- However, as these assets could be drawn down over time for other purposes, staff's examination of reserve adequacy (Annex I) also compares reserves excluding FRD deposits with several reserve metrics. Even excluding these deposits, Uzbekistan's



- reserve position is very strong.

  <u>Excerpts from BPM6</u>

- "6.64 Reserve assets are those external assets that are readily available to and controlled by monetary authorities for meeting balance of payments financing needs, for intervention in exchange markets to affect the currency exchange rate, and for other related purposes (such as maintaining confidence in the currency and the economy, and serving as a basis for foreign borrowing)."

- "6.75 An existing asset that is committed for a future use but not encumbered can be included provided that the asset is readily available to meet a balance of payments financing need (and other related purposes stated in paragraph 6.64). An asset should not be denied as a reserve asset simply because the use to which the asset is to be put is a foreseeable one."

- "6.95 If the special purpose government fund's external assets are on the books of the central bank, or an agency of the central government, that allows the monetary authorities control over the disposition of funds, then the presumption is that the assets are reserve assets (provided all other criteria for being a reserve asset are met)."

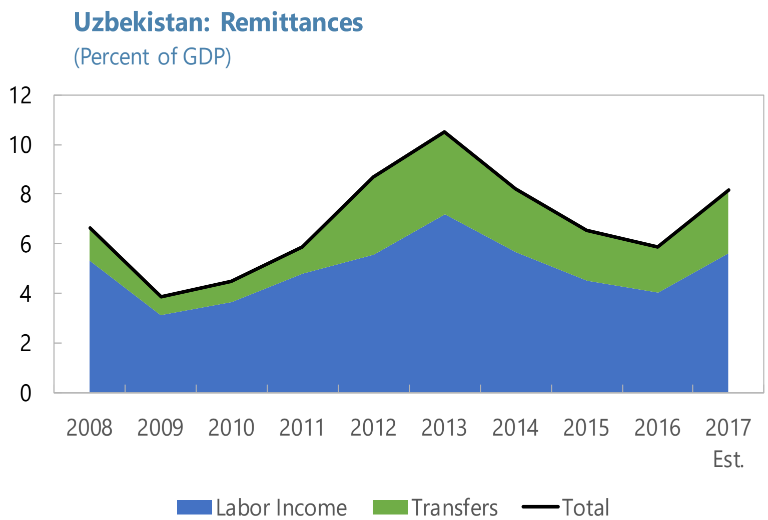
25. What is the nature of controls on capital flows that Uzbekistan has in place and could they be supplemented effectively by macro-prudential measures?

- While Uzbekistan has lifted restrictions on current account transactions, it still maintains a range of controls on the capital and financial account. These include restrictions affecting investment securities, derivatives, commercial and financial credits, direct investment, real estate transactions, commercial banks and institutional investors (as documented in the 2016 Annual Report on Exchange Arrangement and Exchange Restrictions).

26. Given the role of remittances for the balance of payments, we would be interested in the estimates of these flows since the middle of the 2000s, and not just in the U.S. dollar terms, but also as a percentage of GDP.

- Since 2008, remittances from Uzbekistan citizens abroad has ranged from 4 to 13 percent. The peak was reached in 2013 and currently stands at about 8 percent of GDP.

- Between 60-80 percent has come from labor income from seasonal workers while the remainder has come from transfers from non-resident Uzbekistan citizens.



27. Paragraph 13 asserts that "current transactions" can be conducted "without impediment." Can staff confirm that all individuals and entities can freely buy foreign currency in cash, instead of receiving it on a special "conversion card" to be used only abroad?

- Resident individuals may freely purchase foreign exchange using international bank payment cards. Since April 1, 2018, resident individuals are allowed to withdraw cash foreign currency in Uzbekistan from their international bank payment cards within any limits that may be established by commercial banks. Therefore, in practice there is no limitation on obtaining foreign currency in cash.

- In addition, such cards may be freely used for international transactions both within Uzbekistan (such as online purchases) and abroad. The requirement to use a bank card for purchasing foreign exchange does not apply to entities.

28. On the authorities' plan to adopt the inflation targeting, we agree that the central bank should improve its independence and communication strategy. In this regard, we see merit in the Fund providing technical assistance if needed. Can staff comment?

- In the last 6 months, two technical assistance missions on (i) the monetary policy framework and (ii) monetary and foreign exchange operations have provided extensive advice regarding the transition to inflation targeting and operations in the near term.

- For FY19, follow up TA is being considered regarding the monetary framework, monetary policy implementation, and foreign exchange policy implementation.

Financial Sector

29. This plan should include the transformation of state banks' business model to a more commercially-oriented one, including mergers and privatization options, strong regulatory and supervisory frameworks, a bank resolution framework based on best practices and international standards to reduce moral hazard and an effective lender of last resort mechanism. Can staff elaborate on the plan contemplated by the authorities?

- First, modernizing the prudential framework will require a significant and sustained effort over the coming years. There are about 300 prudential regulations in force at this point, and bringing them up to more modern standards will focus first on regulations covering bank capital, liquidity, and asset classification.

- On capital, the regulation on capital adequacy requirements will strengthen the information value of CARs by ensuring better reflection of risks to capital, especially credit risk. The risk-weighted bucket will be adjusted for different credit risk exposures to ensure that risks are properly reflected in CARs.

- On liquidity, the amendments to the regulation on liquidity will ensure better quality of banks' liquid assets. The amendments will also reduce the possibility of manipulating the liquidity ratio through interbank transactions.

- On asset classification, amendments to the regulation will improve the capacity of banks to identify potential losses related to credit risk at an early stage. The number of quantitative and qualitative indicators that are considered by banks for the assessment of credit risk will be increased.

- Other priorities regarding modernizing the regulatory framework for banking in Uzbekistan include drafting new regulations on corporate government and risk management.

30. What is the percentage of loans of public and private banks? How prepared is the private banking sector to deal with credit and capital requirements? The staff's responses are welcome.

- As noted in the staff report, state banks dominate the financial system in Uzbekistan. Private banks, including foreign ones, accounted for less than 15 percent of total loans in 2017. Most of them are relatively small and consolidation in the sector is likely, as banks merge to fulfil capital requirements and gain competitive advantage.

31. Going forward, banks will need more funding and capital to adequately support higher growth and job creation. In this regard, while we also believe that banks should rely on more market-based solutions, such as attracting foreign funding and more deposits from household, instead of FRD funds, what would be an obstacle to take the direction?

32. What can be done to raise attractiveness of Uzbekistan to foreign banks?

(Response to two previous questions.)

- In staff's view, an important obstacle to attracting foreign funding is the dominant role of the state in an overregulated economy which leaves little room for competition.

- The current model involves large state banks providing financial services to SOEs, often at preferential rates, taking advantage of cheap FRD funding. This makes it difficult for private banks, which work on market terms, to compete for clients.

- As for attracting household deposits, high dollarization and low trust in the banking system are key factors. The use of cash foreign exchange is widespread, not just as a store of value but also in transactions.

33. We agree with staff's recommendation that banks should rely more on funding from households' deposits. To this end, we invite staff to share their view based on cross-country experiences on how to attract more deposits from households.

- Increasing the level of trust in the domestic banking system and government's policies are essential for attracting more deposits from households.

- Deposit insurance schemes are being used to ensure that depositors' savings are protected and boost the confidence in the banking system. These schemes differ in terms of coverage limits, participation and funding. Uzbekistan's deposit insurance fund is rather generous in terms of coverage limits as it provides full guarantees on deposits, so the necessary arrangements are there.

- However, for an insurance scheme to fulfill its purpose, it has to be credible, and credibility can be enhanced through ensuring the fund's independence, increased transparency about its financial status and operations, and improved communications to educate the public.

34. Can staff elaborate on the liberalization's effects given the high loan dollarization?

- Loan dollarization has been relatively high in Uzbekistan, reflecting the role of FRD operations (mostly in USD) in the banking system. The share of FX loans increased significantly after the liberalization—to 58 percent at the end of 2017—due to the exchange rate depreciation. Banks generally benefited from the depreciation since they had open positions in FX and part of their capital was denominated in foreign currency.

- SOEs, on the other hand, incurred balance sheet losses and those with revenues primarily in local currency faced difficulties servicing their obligations. The authorities addressed the issue by restructuring loans to domestic banks, postponing the debt payments falling due in 2017-2018 and providing government guarantees.

Structural Reforms

35. ***We take note that the authorities took steps to improve the business environment in line with Fund's recommendations to reform the investment climate. Can staff please elaborate on the implemented measures? We would also appreciate staff's view on the issues of governance and corruption in Uzbekistan which are not mentioned in the report.***

- Between 2015 and 2018, Uzbekistan's Doing Business rank rose from 141 to 74. Areas of particular improvement included starting a business (from 65 to11), registering property (143 to 73), and getting electricity (145 to 27).

- The Doing Business survey is based on de jure measures and may not reflect other impediments to investment. the staff's discussions with the private sector indicates they are hopeful that reforms will result in significant improvement in the business environment, but some investors expressed a wait and see attitude.

36. ***Do staff consider corruption to be a macro-critical issue for Uzbekistan? If so, we encourage them to provide analysis of its impact in the next Article IV.***

(Response to two previous questions.)

- Corruption and governance issues are macro-critical.

- In fact, the government's policy agenda puts improving the quality of institutions front and center (see SR paragraph 4 on the policy agenda, especially the objective of enforcing the rule of law by an independent judiciary).

- As regards corruption specifically, as noted in the SR (paragraph 43), the government's plan of specific actions to implement the policy agenda lists the fight against corruption as a key priority (action #64), including improving anti-corruption legislation. The deadline for implementing this action is November 2018.

- Given the authorities' intentions and that the next Article IV will probably take place in Spring 2019, the next Article IV could indeed be a good time to take stock on this topic in line with the recently approved framework for Fund enhanced engagement on governance.

GDP, Growth, and Employment

37. ***The selected economic indicators (table 1) show a significant drop in the GDP per capita expressed in U.S. dollars between 2016 (2,094) and 2017 (1,491). Even though this evolution can be explained by the devaluation, the figure for 2017 still***

seems low. Could staff comment on the presented figures and on whether a GDP rebasing exercise is considered by the authorities?

38. We note in Table 1 that the estimated GDP per capita (in U.S. dollars) has decreased sharply after depreciation. Is it possible to present the GDP per capita in real terms, that is, in PPP? the staff's comments are welcome.

(Response to two previous questions)

- The drop in GDP per capita in U.S. dollars is entirely driven by the exchange rate changes. The annual average exchange rate increased by 75 percent. The growth in nominal and real GDP in Soms remain positive.
- The IMF estimates Uzbekistan's PPP GDP per capita at $7,350, slightly below India and Vietnam.
- The level of nominal GDP is likely underestimated as estimates of non-observed economy are not produced. Adjusting for non-observed sectors would likely raise the level of GDP by at least 20 percent.

39. We believe that during the period since 1995 used by staff in Figure 1, the average annual growth of the Uzbek real GDP per capita was almost 5 percent. Can staff confirm this number? More clarity would be useful to better understand staff's arguments about the pace of reforms envisaged by the authorities.

40. Could you, please, clarify, what is the definition of "reaching upper middle-income status"? How do we measure this goal? And what does it mean for Uzbekistan "to fall increasingly short of" this goal? What should happen in terms of growth/exchange rates/definitions for Uzbekistan to reach this goal by 2030, as it was suggested by Ms. Barron?

(Response to two previous questions)

- From 1995 to 2016, growth in real GDP averaged 6.5 percent, while growth in total U.S. dollar GDP averaged 9.4 percent. With rising population, growth of GDP per capita in U.S. dollars was lower at 6.4 percent.
- In 2017, Uzbekistan's GDP per capita was about $1,500. The World Bank defines upper middle-income economies as those whose GNI per capital ranges from $4,036-$12,475. Thus, to reach the lower end of this range by 2030, U.S. dollar GDP would need to grow at a rate of 8.0 percent over the next 13 years. This represents an increase over the historical rate, but has occurred in other reforming economies.

41. ***Could staff explain this low relationship between GDP growth rate in recent years and the growth rate of employment?***

42. ***Could the staff elaborate the reasons behind the stagnation in job creation? What is the staff assessment of Uzbekistan's institutional and human capacity which will help it to reap the demographic dividend? Also, in addition to providing jobs, how do the authorities plan to ensure safety and security of labor in the workplace, both domestic and migrant? Could staff comment on the possible use of available fiscal space in this domain?***

43. ***Considering the limited success of past policies in creating jobs, can staff elaborate on the plans to generate adequate employment?***

(Response to previous three questions)

- The reasons for poor growth of employment are unclear. One factor may be a tax system that increases the tax burden on firms that grow beyond a set threshold. Another may be a heavily regulated economy that makes it harder for individuals and firms to engage in new activities.

- Uzbekistan's population is well educated (as illustrated by the almost 100 percent adult literacy rate) and has significant human capacity. Reforms, including liberalizing prices and promoting domestic competition, should help to open new economic activities and thus foster job creation.

Other Issues

Delayed Article IV Consultations

44. ***We take note that both the last and the present Article IV consultations have been delayed. Could staff provide information on the reasons for repeated delays in completing Article IV consultations with Uzbekistan?***

45. ***Three years ago, staff intended to return to the normal 12-month surveillance cycle, but it did not happen. We ask staff to explain the reasons for the repeated major deviations from the established Fund policies.***

46. ***As the proposed Article IV consultation in 2015 should have held on the standard 12-month cycle, we would like to the ask staff the reasons for such a delay.***

- Questions on delayed Article IV consultations to be answered orally.

Format of Article IV Report

47. We also note that the report is again very brief and it is not accompanied by a selected issues paper. Given the recognition of the magnitude of possible changes in Uzbekistan's policies, the absence of supporting research is especially regrettable. We would appreciate staff's explanation on the reasons for their choice of format for the Article IV report and on whether any research is planned on this large economy facing complex policy challenges and undergoing systemic reforms.

- Given the length of time since the last Article IV consultation and significance of ongoing reforms in Uzbekistan, staff concentrated its efforts on evaluating economic developments, understanding the authorities plans and the impact of reforms, and intensive dialogue with the authorities.

- the staff agrees that given the magnitude of reforms, there are many topics which merit future research; for example, the monetary transmission mechanism, the likely impact of tax reform, restructuring of state enterprises, and lessons from other reform experiences. the staff hopes to examine these issues in the near future.

Publication

48. Why the authorities have not yet consented to the publication of the staff report?

49. As the discussed report (and its overall positive remarks) could constitute a useful tool to attract additional investment, we invite authorities to consider its timely publication and would like to ask the staff if any indication was provided since the circulation of the report.

(Response to previous 2 questions)

- When the report was issued to the Board, the authorities indicated they were undecided on publication.

- The authorities are best placed to explain their views on publication.