



CONTEMPORARY TRENDS IN BALANCE OF PAYMENTS OF UZBEKISTAN AND REGULATION POLICIES

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Abstract

The article shows various opinions related to the essence of the balance of payments, explores the relationship between the balance of payments and economic growth. It analyzed the items of the balance of payments of Uzbekistan and identified the factors that influence them. A methodological approach to the analysis of the balance of payments is proposed, which differs from the traditional comprehensive assessment, which allows a comprehensive study of the balance of payments. The methodological basis of the study was the dialectical method of cognition and the systematic approach. In the course of the research, such scientific techniques and methods were used as abstraction, “from the abstract to the concrete”, a combination of analysis and synthesis, induction, deduction, comparison methods, a combination of historical and logical methods, which made it possible to improve the quality of work and deepen the problems under study. In addition, it provides proposals and recommendations aimed at regulating the country’s balance of payments.

Keywords: Balance of payments, devaluation, balance of goods and services, capital account, gold and foreign exchange reserves

INTRODUCTION

Indicators of the balance of payments play an essential role in the selection and use of methods for regulating foreign economic activity aimed at promoting or restricting foreign economic operations in reliance upon the country’s international settlements, as well as currency and

economic situation. Herewith, the analysis of the residual of the balance of payments is required to determine economic policy.

“The Action Strategy for five priority areas of the development of the Republic of Uzbekistan for 2017-2021” approved by the Decree of the President of the Republic of Uzbekistan PD-4947 “On the Action Strategy for further development of the Republic of Uzbekistan” as of February 7, 2017 determines “further strengthening macroeconomic stability and maintaining high economic growth rates” in terms of economy development and liberalization”. Further development of international economic cooperation, including expanding relations with leading international and foreign financial institutions, continuing to pursue a well-thought-out foreign debt policy, efficient use of attracted foreign investment and loans; further improvement of monetary policy applying the instruments used in international best practices, as well as the gradual introduction of modern market mechanisms in currency regulation, ensuring stability of the national currency are among the high-priority objectives within this priority area.

It should be noted that the balance of payments has its individual peculiarities for each country, and this is justified by the economic policy of that country, its economic development and economic security, resource supply, and etc. Moreover, the balance of payments is under a significant impact of the international environment and conditions.

LITERATURE REVIEW

The analysis of government measures implemented to solve the problems with the balance of payments proves that the first step is to apply the measure to sell foreign reserves, and if these measures do provide urgent effect, then it is required to introduce the forms of capital oversight. The same situation is applicable to the devaluation: governments first apply smaller devaluations and higher interest rates, and if this does not bring about proper expected outcomes, they have to implement large-scale devaluations [Lawrence *et.al.*, 2016].

However, while the devaluation policy will temporarily improve the balance of payments, it will not enable the balance of payments to improve on a sustainable basis without appropriate domestic monetary policy [Guitian, 1973].

Moreover, governments follow a certain sequence in resolving the problems with a balance of payments, that is, they first undertake measures that do not require considerable expenditures and efforts, and then shift to the cost-based measures only if the problem solution is not as efficient as expected.

P. Krugman considers an export-oriented economic growth strategy based on the dependence of the national currency of China to the USD below parity as a crucially important factor in the emergence of the deficit of the US balance of payments [Krugman, 2010].

From the point of view of some analysts, the decline in the ratio of the US National Fund rate to the investment rate will play a pivotal role in the growth of the deficit in the USA. As long as the savings rate in the USA does not increase, the country will continue to receive huge amounts of capital, which, in turn, will cause a current account deficit. High levels of savings reduce consumption and thus trade deficits [Raheja, 2010].

In accordance with the hypothesis of “global surplus of funds”, the major cause for the balance of payments deficit is the emergence of surplus funds from developing countries. The US economy, in turn, is attracting these “surplus funds” [Bernanke, 2005].

In the opinion of some economists, the difference between the return of the USA in foreign investments and the return on foreign investments in the USA provides this country with a positive investment balance and promotes a large foreign trade deficit. Between 1952 and 2009, the return of the USA in foreign investments was 2.69% higher than the return on foreign investment in the USA. In addition, this figure increased from 1.3 percent in 1952-1972 up to 3.47 percent in 1973-2009 [Gourinchas et al., 2010].

M. Feldstein points out that there may be a risk in changing the nature of the financing of the current account deficit in the United States. At the beginning of the first decade of the 21st century, the deficit was stable because it was financed by private investors, which, in turn, resulted in private investment income and yielded efficiency to the American economy. By the end of the decade, the capital inflow into the US economy occurred after foreign governments were actively buying up debt obligations of the USA. For the United States, which in many respects relies on foreign purchases of treasury bonds, a sudden change in the economic situation could have negative [Feldstein, 2008].

ANALYSIS AND DISCUSSIONS

During the years of independence, the issue of ensuring a positive (active) balance of payments in Uzbekistan has been considered a crucially important prerequisite for macroeconomic stability. As a result, the country maintained a moderate level of external debt, gave priority to attracting foreign direct investment in key sectors of the economy, as well as ensured that imports are entirely covered by exports, i.e. there is absence of the balance of trade deficit as the basic indicator for foreign economic activity.

In the last two years, the current account in Uzbekistan demonstrates deficit (except for the quarter 3 of 2019).

Table 1 The structure of the balance of payments of the Republic of Uzbekistan

In million USD

No	Sections of balance of payments	Quarter 1 of 2018	Quarter 2 of 2018	Quarter 3 of 2018	Quarter 4 of 2018	Quarter 1 of 2019	Quarter 2 of 2019	Quarter 3 of 2019	Quarter 4 of 2019	Quarter 1 of 2020
I	Balance of current account	-225,65	-1374,81	-1546,59	-446,65	-1049,90	-708,20	39,17	-1508,90	-812,18
1.1	Balance of goods	-770,86	-2168,89	-2512,39	-1414,72	-1696,74	-1877,56	-1382,04	-2334,98	-1578,99
1.2.	Balance of goods and services balance	-1340,70	-2730,57	-3178,94	-2058,20	-2250,78	-2399,95	-1989,37	-2917,28	-2038,04
II	Balance of capital account	-197,53	-1369,59	-1476,89	-406,65	-914,78	-673,59	116,31	-1501,76	-812,03
III	Financial account	-412,19	-145,86	-154,69	-698,54	-2206,14	-2241,03	-1190,33	-2219,47	-719,71

Source: Central Bank of the Republic of Uzbekistan

In 2018-2019, balance of goods in the country during all quarters of the fiscal year was negative, i.e. imports of goods exceeded its exports. It should be noted, that the same situation was observed with export and import of the services. As a result, the balance of goods and services in the analyzed period was only in deficit. Reducing the balance of payments deficit can be practically achieved by raising the revenues or reducing payments, as well as by increasing the rate of revenues against the rate of payments or reducing the rate of revenues against the rate of payments. This requires paying particular attention to two important aspects of the balance of payments, namely its monetary nature and the general economic situation.

Therefore, the government has to select one of the economic policy supports or their appropriate combination. In our opinion, currently it is essential to prioritize the accumulation of gold and foreign exchange reserves in order to eliminate the balance of payments deficit. This is because the reserves cover the deficit and provide more freedom in policy choice.

Herewith, the deficit of the balance of payments is the result of a negative balance of trade, and if this situation is the result of an increase in imports of the advanced equipment and machinery in order to raise production capacity, its impact on the economy could be positive. On the other hand, if to take into consideration excessive consumption of non-investment goods, then the long-term impact on the economy is expected to be negative. Herewith, if the current account deficit is based on a negative balance of income, then the country must solve the problem of external debt.

The analysis of the composition of foreign investors in the economy of Uzbekistan demonstrates that the major foreign investors in the economy of our country are the Russian Federation, the Republic of Korea and the People's Republic of China. In recent years, the share of the Republic of Korea in total foreign investment in our national economy has grown significantly. In 2015, the Republic of Korea with a share of 30.5% became the largest foreign investor in Uzbekistan. The opposite scenario with the share can be witnessed in the People's Republic of China. Thus, in 2010 the share of the People's Republic of China in foreign investment in the economy of Uzbekistan constituted 48.6%, in 2016 this indicator declined significantly and amounted to 14.8%. Meanwhile, the share of the Russian Federation as a foreign investor has demonstrated a dynamic character because the Russian Federation was the major foreign investor in Uzbekistan in 2007, 2011, 2014 and 2016.

Relevant competent public authorities may undertake various measures to solve the problems with a balance of payments, such as a sharp decline or complete cessation of capital inflows and a huge foreign trade deficit. In particular:

- selling foreign exchange reserves to maintain the value of the national currency;
- raising interest rates to promote the foreign capital inflow into the country;
- introducing the capital control forms against the sale of domestic assets;
- application of a combination of import tariffs and export subsidies in order to reduce domestic demand and promote exports;
- devaluation of the national currency.

However, taking into consideration that the above measures complement or substitute each other, it is crucially important to select the most optimal one or to determine their optimal combination.

In our opinion, it is essential to arrange activities in two areas in attracting foreign investors into the national economy within the framework of incomplete liberalization of foreign exchange transactions on the capital inflow into our country: First, by obtaining a sovereign credit rating of the country, it is possible to clarify the level of risk for foreign investors and, consequently, to assess the expected level of return. Second, it is recommended to enhance the share of foreign investors in joint-stock companies and other organizational - legal forms of management, as well as to ensure participation of foreign investors in the management of these companies and to supervise their management.

If the issue of the full liberalization of the capital flow represents urgency in the long-term prospective, ensuring free foreign exchange on current operations will be essential not only for the foreign trade development, but also for the profit repatriation of the investments made in the national economy. If officially the foreign exchange on international currency operations was

implemented until October 15, 2003, in practice, there were delays in import-limiting foreign exchange operations and there existed a number of restrictions on the sale and purchase of foreign currency in the over-the-counter interbank foreign exchange market. As a result, there was a significant difference between the informal parallel market rate (the “black market” rate) and the official exchange rate. This, in turn, negatively affected investment attractiveness of the national economy, in particular, modernization processes in the leading sectors of the economy due to delays in the import of machinery and equipment.

Bringing the development of our country to a new level requires a reconsideration of the monetary policy pursued so far, its liberalization in reliance upon advanced world experience and market mechanisms. The Decree of the President of the Republic of Uzbekistan PD-5177 “On priority measures to liberalize foreign exchange policy” dated September 2, 2017 was crucially important step in this area. This Decree determined the priorities of the government economic policy in the field of further liberalization of the foreign exchange market in the country. These priorities include such urgent measures of the top priority which must be undertaken by the government as ensuring full realization of the right of legal entities and individuals to freely buy and sell foreign exchange and to freely dispose of their funds at will, enhancing the role of market instruments in the use of foreign exchange resources, creating equal conditions for all businesses in the foreign exchange market, raising increase the stimulating role of monetary policy in the development of exports in non-traditional sectors, strengthening regional and international economic cooperation, as well as effective operation of enterprises in key sectors in the new conditions of foreign exchange.

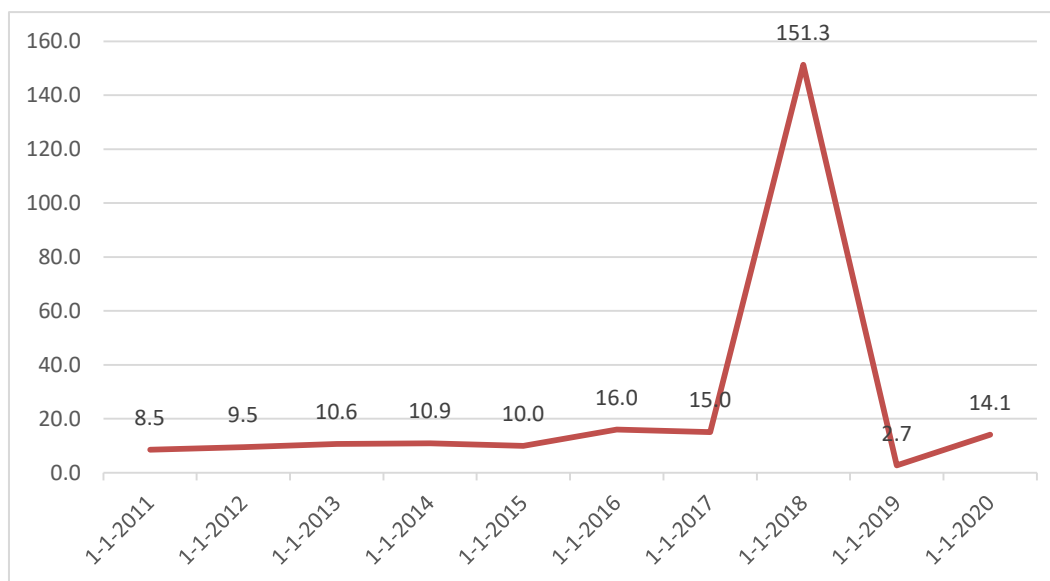


Figure 1. The devaluation rate of the UZS against the USD, in%

Source: Central bank of the Republic of Uzbekistan

Since September 5, 2017, the Central Bank of the Republic of Uzbekistan set the official exchange rate of the UZS against the USD at 8100.0 UZS for 1 USD. This illustrates a high rate of devaluation of the UZS, which constituted 92.4%. Relatively stable exchange rates were recorded during 2018 after the monetary policy liberalization (see Figure 1). This year, the national currency devaluation against the USD amounted to 2.7%. However, from 2019 the devaluation rates of the UZS approached the rates of the period before the monetary policy liberalization.

It should be noted that the Government of Uzbekistan has urgently commenced to mitigate the effects of the introduction of free foreign exchange conversion and developed effective measures. In particular, appropriate measures have been undertaken to raise the level of capitalization and liquidity of commercial banks, support basic sectors of the economy, prevent a sharp rise in prices for socially important goods and with the account of rising inflationary pressures the Central Bank increased a refinancing rate from existing 9 percent to 14 percent.

Herewith, reliance on market mechanisms in the formation of the exchange rate of the UZS against the leading foreign currencies in the foreign exchange market may result in the increase in exchange rate fluctuations, as it fully responds to the liberalization policy in the foreign exchange sector. This requires the Central Bank to be able to influence supply and demand in the foreign exchange market in order to prevent sharp fluctuations in exchange rates and to provide adequate foreign exchange assets for this purpose.

CONCLUSION AND RECOMMENDATIONS

In our opinion, within the framework of the economy liberalization, it is necessary to take into consideration the following aspects when developing the measures to regulate the balance of payments:

- it is necessary to undertake appropriate measures to maintain a constant surplus of the balance of payments. In particular, to prevent the trade deficit in Uzbekistan, enhance export potential of the national economy, raise the share of high value-added science-intensive goods and services in exports, it is required to introduce digital technologies in business processes and management, as well as search for promising markets and find efficient ways to enter them;
- The Central Bank of the Republic of Uzbekistan is required to support the policy of not exceeding the real exchange rate of the UZS against the currencies of major trading partners, and in this process regularly monitor the impact of the exchange rate on the balance of payments and its components;

- It is recommended to ensure adequacy and efficient management of gold and foreign exchange reserves. Foreign exchange reserves must be adequate for the central bank to be able to significantly influence supply and demand in the foreign exchange market if necessary;
- Moderate foreign debt policy should be followed in financing the state budget deficit and foreign trade deficit;
- It is necessary to develop national capital market instruments in order to further expand attraction of foreign investment in the national economy. In particular, in order to protect foreign investors from currency risk, it is required to arrange the issuance of foreign currency securities by local companies.

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