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Ways to Further Improve the Activities of Banks in the Financial Market in Uzbekistan

Yuldashev Farxodbek Abdumutalibovich [1]

[1] Tashkent State economic university, senior lecturer in the Department of "specialist Sciences", PhD.

Abstract:

This paper examines potential strategies for enhancing the role and performance of banks in the financial market of Uzbekistan. Through a comprehensive literature review and analysis, it identifies key challenges facing the Uzbek banking sector and proposes a set of policy recommendations to improve the efficiency, stability, and development impact of banks. The main findings highlight the need for continued financial sector liberalization, strengthening of regulatory and supervisory frameworks, promotion of competition and consolidation in the banking industry, expansion of financial inclusion and access to credit for underserved segments, and development of capital markets as a complementary source of long-term financing.

Keywords: Uzbekistan, banking sector, financial markets, liberalization, regulation, financial inclusion.

INTRODUCTION

Since gaining independence in 1991, Uzbekistan has pursued a gradual approach to economic transition characterized by cautious financial sector reforms [1]. While this approach helped avoid the instability experienced in some other former Soviet economies, it also constrained the pace of financial development. The banking sector remains dominated by state-owned banks, with limited foreign participation and private sector credit [2]. Financial markets are shallow, with a nascent securities market and heavy reliance on bank financing. Recognizing the need for a more efficient and competitive financial system to support its economic modernization goals, the government has recently accelerated financial sector reforms [3].

The financial sector plays a crucial role in economic development by mobilizing savings, allocating capital, and facilitating risk management. Banks, as the dominant financial intermediaries in most emerging markets, are at the forefront of this process. Efficient and stable banking systems can support investment, innovation, and productivity growth, while underdeveloped or dysfunctional ones can hinder economic progress. In the context of transition economies, developing a sound and inclusive banking sector is particularly important for enabling private sector development and economic transformation.

This article aims to contribute to the ongoing policy dialogue by identifying ways to further improve the activities of banks in the financial market in Uzbekistan, drawing on international experience and considering the specific country context. It argues that enhancing the role of banks requires a comprehensive and coordinated reform agenda that addresses multiple interrelated challenges, including state ownership, regulatory frameworks, market structure, financial infrastructure, and institutional development.

METHODS AND LITERATURE REVIEW

This article relies on a qualitative methodology involving an extensive review of academic literature, policy reports, and statistical data related to the Uzbek financial sector. It analyzes the current state and evolution of the banking industry and financial markets in Uzbekistan, benchmarking against regional peers and international standards. The literature review covers several strands of research relevant to the topic. First, it examines studies on the relationship between financial sector development and economic growth, which find that deep and efficient financial systems are critical for channeling savings to their most productive uses and supporting capital accumulation, productivity growth, and innovation [4]-[6]. Second, it reviews cross-country empirical evidence on the determinants of financial sector development, highlighting the importance of macroeconomic stability, institutional quality, legal and regulatory frameworks, market structure, and financial infrastructure [7]-[9]. Third, it considers the specific challenges facing transition economies in developing market-based financial systems, including the legacy of state ownership, weak governance, limited competition, and underdeveloped capital markets. Finally, it draws on policy literature outlining strategies for financial sector reform in emerging markets, emphasizing the need for a holistic and sequenced approach tailored to country circumstances.

RESULTS

The analysis reveals several key challenges and opportunities for improving the activities of banks in the financial market in Uzbekistan. First, despite progress in privatization and liberalization, the banking sector remains dominated by state-owned banks, which account for over 80% of total assets [10]. State ownership can lead to inefficiencies, politicized lending, and crowding out of private banks. Second, foreign participation in the banking sector is limited, with only a handful of foreign banks operating in the country. Greater foreign investment could bring much-needed capital, expertise, and technology to the sector. Third, access to finance remains a constraint for many firms, particularly small and medium enterprises (SMEs) and those in rural areas. Expanding financial inclusion through innovative products, alternative delivery channels, and improved credit information systems could help address this gap. Fourth, the level of financial intermediation is low, with private sector credit to GDP ratio of around 30%, well below the average for lower-middle-income countries [11]. Strengthening the legal and regulatory framework for secured transactions, insolvency, and contract enforcement could help boost lending. Fifth, capital markets remain underdeveloped, with a small stock market and limited corporate bond issuance. Developing a wider range of financial instruments and institutional investors could provide a valuable complement to bank financing.

ANALYSIS ANS DISCUSSION

The results of the analysis suggest several policy priorities for enhancing the role of banks in the financial market in Uzbekistan. First, the government should continue to pursue privatization and reduce the state's share in the banking sector, while strengthening governance and oversight of remaining state-owned banks. Attracting strategic foreign investors could help bring international best practices and foster competition. Second, the Central Bank should continue to strengthen the regulatory and supervisory framework, with a focus on risk-based supervision, consolidated monitoring of banking groups, and enhanced macroprudential tools to manage systemic risks. Third, policies should aim to promote greater competition and efficiency in the banking sector, including through licensing of new banks, removal of entry barriers, and incentives for consolidation and mergers of smaller banks. Fourth, expanding financial inclusion should be a key priority, with a focus on developing microfinance, digital financial services, and targeted SME lending programs. Improving credit information systems and collateral registries could help mitigate risks and expand access to finance. Fifth, developing domestic capital markets should be a medium-term goal, starting with reforms to strengthen the legal and regulatory framework, build market infrastructure, and promote institutional investors such as pension funds and insurance companies.

Implementing these reforms will require strong political will, coordination among government agencies, and consultation with private sector stakeholders. It will also be important to carefully sequence reforms, prioritizing measures to strengthen the enabling environment and build capacity before fully liberalizing the sector. Policymakers can draw on the experience of other transition economies and emerging markets that have successfully pursued financial sector reforms, while tailoring strategies to the specific needs and circumstances of Uzbekistan.

CONCLUSION

Uzbekistan has made significant strides in reforming its financial sector in recent years, but further efforts are needed to enhance the role of banks in supporting private sector development and economic growth. By pursuing a comprehensive reform agenda focused on privatization, regulation, competition, inclusion, and market development, policymakers can help unlock the potential of the banking sector to efficiently intermediate savings and allocate credit to productive investments. While challenges remain, the current momentum for reform and the country's strong economic fundamentals provide a favorable environment for pursuing these changes. Further research could focus on assessing the impact of specific reforms, identifying remaining gaps and constraints, and benchmarking Uzbekistan's progress against peer countries. Strengthening the financial sector will be critical for achieving Uzbekistan's goal of becoming an upper-middle-income country by 2030 and ensuring sustainable and inclusive growth in the years to come.

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