

AN ASSESSMENT OF THE INVESTMENT CLIMATE AND ITS ROLE IN
ATTRACTING FOREIGN DIRECT INVESTMENT IN UZBEKISTAN

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ABSTRACT

This article provides a comprehensive assessment of Uzbekistan's investment climate and examines its effectiveness in attracting foreign direct investment (FDI) amidst the country's ongoing economic transformation. Since 2017, Uzbekistan has implemented wide-ranging reforms aimed at liberalising its economy, modernising the legislative framework, and improving the business environment. Drawing on recent data from international financial institutions and empirical studies, this paper analyses FDI trends, the legal and institutional framework for investment, and the remaining challenges that constrain foreign capital inflows. The findings indicate that while FDI has grown significantly—reaching USD 2.2 billion in 2023—it remains concentrated in capital-intensive sectors such as energy and manufacturing, with limited diversification by origin and geography. Foreign-owned firms demonstrate labour productivity 63.8% higher than domestic enterprises and contribute positively to exports, innovation, and skills development. However, spillover effects to the broader economy are constrained by regulatory uncertainty, institutional fragmentation, and limited absorptive capacity among local small and medium-sized enterprises. The article concludes with policy recommendations to enhance the investment climate, including strengthening the investment promotion agency, reducing regulatory unpredictability, and fostering greater linkages between foreign investors and domestic firms.

Keywords: foreign direct investment, investment climate, Uzbekistan, economic reforms, investment promotion, institutional framework.

1. INTRODUCTION



Foreign direct investment has long been recognised as a critical catalyst for economic development in transitioning economies. For landlocked developing countries, FDI serves not only as a source of capital but also as a vehicle for technology transfer, managerial expertise, integration into global value chains, and employment generation (Borensztein et al., 1998; Alfaro et al., 2004). In the context of Uzbekistan—the most populous nation in Central Asia with over 36 million people and a strategically advantageous position along historic trade routes—attracting sustainable and diversified FDI has become a central pillar of national development strategy.

Since 2017, Uzbekistan has embarked on an ambitious reform agenda unprecedented in its modern history. Following decades of relative isolation and state-dominated economic management, the government initiated comprehensive liberalisation measures including foreign exchange regime reform, price liberalisation, simplification of business registration procedures, and the adoption of modern investment legislation. The Development Strategy of New Uzbekistan for 2022–2026 explicitly targets increasing FDI inflows to USD 70 billion over five years, reflecting the elevated priority accorded to foreign investment in national planning.

However, despite notable progress, Uzbekistan's ability to attract and, critically, to leverage foreign investment for sustainable development faces persistent challenges. FDI stocks remain low relative to comparator economies—equivalent to 14.6% of GDP in 2023—and inflows are heavily concentrated in extractive industries and manufacturing, with Chinese and Russian investors accounting for the largest shares. Moreover, the spillover benefits that typically accompany foreign investment, such as productivity enhancements in the domestic sector and technology diffusion to local firms, have yet to materialise fully.

This article assesses the current state of Uzbekistan's investment climate and evaluates its effectiveness in attracting foreign direct investment. It addresses three principal research questions: First, what are the key trends and characteristics of FDI inflows to Uzbekistan since the reform period began? Second, how do the legal, institutional, and policy frameworks shape investor decisions? Third, what obstacles continue to impede greater and more beneficial FDI, and how might these be addressed?

The article proceeds as follows: Section 2 reviews the theoretical and empirical literature on FDI determinants in transition economies. Section 3 analyses recent FDI trends in Uzbekistan. Section 4 examines the legal and institutional framework for investment. Section 5 identifies persistent challenges, and Section 6 concludes with policy recommendations.

2. LITERATURE REVIEW: DETERMINANTS OF FDI IN TRANSITION ECONOMIES

The theoretical foundations for understanding FDI location decisions are well established in the international business literature. Dunning's eclectic paradigm (OLI framework) posits that firms engage in foreign investment when they possess ownership-specific advantages (such as technology or brand equity), when location-specific factors in the host country are favourable (market size, resource endowments, policy environment), and when internalisation advantages make cross-border ownership preferable to licensing or contracting.

For transition economies specifically, the empirical literature has identified several categories of determinants. Macroeconomic stability, reflected in sustained GDP growth and



manageable inflation, provides the foundational confidence required for long-term investment commitments. Institutional quality—encompassing regulatory transparency, contract enforcement, property rights protection, and corruption control—has emerged as particularly critical for countries moving from state-dominated to market-based systems (Globerman & Shapiro, 2003).

Market-seeking FDI responds to population size and income growth, while efficiency-seeking investment is attracted by labour costs and skills availability. For resource-rich economies like Uzbekistan, natural resource endowments predictably draw substantial investment into extractive sectors. However, as Blonigen and Piger (2014) demonstrate, policy factors including tax incentives, trade openness, and investment promotion efforts also exert significant influence.

The experience of other Central Asian and Eastern European transition economies offers pertinent lessons. Carstensen and Toubal (2004) found that privatisation programmes in Central and Eastern Europe drove substantial FDI inflows during the 1990s, a channel historically underutilised in Uzbekistan due to the slow pace of state-owned enterprise reform. Kazakhstan's success in attracting diversified FDI, by contrast, demonstrates the importance of predictable regulatory frameworks and proactive investment promotion.

3. TRENDS AND CHARACTERISTICS OF FDI IN UZBEKISTAN

3.1. Aggregate FDI Flows

Foreign direct investment in Uzbekistan has grown considerably since 2017, although from a low base. According to OECD data, FDI stocks reached an estimated USD 14.9 billion in 2023, equivalent to 14.6% of GDP—a figure that remains modest compared to peer economies in Central Asia and Eastern Europe. Annual inflows averaged 2.8% of GDP over 2019–2023, totalling USD 2.2 billion in 2023. While these flows represent substantial progress, they account for a relatively small share of gross fixed capital formation, which itself is dominated by public investment.

The trajectory of FDI since 2017 reflects the impact of liberalising reforms. Gross fixed capital formation increased from 23.0% to 36.8% of GDP between 2017 and 2019, with private investment gradually gaining ground. Uzbekistan weathered the COVID-19 pandemic and the regional spillovers from the war in Ukraine relatively well, continuing to attract new investment projects despite global headwinds.

3.2. Sectoral and Geographical Concentration

A defining characteristic of FDI in Uzbekistan is its concentration in specific sectors and originating countries. Over 2019–2023, approximately three-quarters of total FDI inflows were directed to manufacturing (41.8%); electricity, gas, and air conditioning supply (20.6%); and mining and quarrying (12.5%). This pattern reflects Uzbekistan's natural resource wealth and the capital-intensive nature of energy and extraction projects.

Major foreign investments include Russia's Lukoil in gas production, the Korea-Uzbekistan joint venture Uz-Kor Gas Chemical, and partnerships with China's BYD for electric vehicle manufacturing. While these projects bring substantial capital and technology, their sectoral concentration raises questions about economic diversification and the inclusiveness of FDI benefits.



In terms of origin, Chinese and Russian investors account for the largest shares, particularly through large-scale energy and infrastructure projects. The potential for greater involvement from OECD countries and other advanced economies remains significant. Recent initiatives such as the Belgium–Uzbekistan Business Forum in November 2025, which brought together European companies from logistics, healthcare, and sustainable technologies, signal growing interest from diversified sources.

Geographically, FDI remains concentrated in regions with extractive resources or established industrial bases, though special economic zones are increasingly influencing the spatial distribution of investment.

3.3. Mode of Entry: Greenfield versus M&A

Uzbekistan's FDI inflows are dominated by greenfield projects rather than mergers and acquisitions. This pattern reflects the historically limited privatisation of state-owned enterprises, which in other transition economies provided a major channel for foreign entry. However, recent privatisation efforts are beginning to change this landscape. Notable transactions include Singapore's Indorama Corporation purchasing the government's stake in fertiliser producer Ferganaazot and Hungary's OTP Bank acquiring Ipoteka Bank in 2023. As privatisation accelerates, M&A activity is likely to increase, offering new opportunities for foreign investors.

3.4. Economic Impacts of FDI

Foreign-owned firms in Uzbekistan demonstrate significantly higher productivity than their domestic counterparts—labour productivity is on average 63.8% higher, though this premium partly reflects sectoral concentration. These firms are also considerably more export-oriented, contributing to Uzbekistan's growing international trade integration.

In the domain of innovation and technology, foreign affiliates are more likely to utilise ICT and internationally licensed technologies, introducing new knowledge and practices to the local economy. However, technology spillovers to domestic firms remain limited by the absorptive capacity of local small and medium-sized enterprises. While domestic firms show some propensity for process innovation, they lag considerably in product innovation and R&D investment.

Employment creation from FDI is moderate relative to investment volumes, reflecting the capital-intensive nature of dominant sectors. Most jobs are created in consumer products, textiles, and automotive assembly. Foreign-owned firms are more likely to provide worker training and pay higher wages than domestic enterprises, contributing to skills development and living standards. Additionally, foreign firms demonstrate greater propensity to employ women, aligning with national gender equality objectives under the National Gender Equality Strategy 2030.

4. THE INVESTMENT CLIMATE: LEGAL AND INSTITUTIONAL FRAMEWORK

4.1. Legislative Foundations

Since 2019, Uzbekistan has fundamentally restructured its legal framework for investment. The Law on Investments and Investment Activity (LOI) of 2019 established core principles including non-discrimination, investor rights protection, and guarantees against expropriation.



This was complemented by the Law on Public-Private Partnerships (2019) and the Law on Special Economic Zones (2020), creating a comprehensive legislative basis for private investment.

However, the frequency of legislative amendments—including a new draft LOI currently under approval—has created challenges for regulatory stability. As the OECD notes, "legislative overproduction, unclear regulatory mandates, and heavy reliance on secondary legislation have contributed to institutional fragmentation and legal uncertainty." Business stakeholders consistently identify regulatory complexity and unpredictability as key constraints.

4.2. Institutional Architecture

The institutional landscape for investment promotion and facilitation involves multiple actors with sometimes overlapping responsibilities. The Ministry of Investment, Industry and Trade (MIIT), established in 2022 through the merger of the State Investments Committee and Ministry of Foreign Trade, serves as the primary government body for investment policy.

The Investment Promotion Agency of Uzbekistan (UzIPA), created in 2019, operates under MIIT with a mandate for investment generation, facilitation, and aftercare. However, institutional ambiguity persists. A recent OECD assessment found that "the function of UzIPA is unclear and insufficiently integrated into national strategies," with MIIT gradually assuming functions traditionally handled by IPAs. UzIPA faces resource constraints that limit its ability to represent smaller investors and implement key initiatives, while decision-making processes between the Cabinet of Ministers, MIIT, and UzIPA lack coherence.

Other institutions play supporting roles. The Chamber of Commerce and Industry facilitates business linkages, while sector-specific bodies such as IT Park promote investment in digital industries. Special economic zones, numbering over 20, offer preferential regimes for investors, though their proliferation raises questions about co-ordination and effectiveness.

4.3. Investment Promotion and Facilitation

Uzbekistan has made notable progress in streamlining administrative procedures. Since 2018, over 20 presidential decrees have sought to simplify licensing and registration processes, and approximately 70% of public services have been automated, with a target of 80%. The government has introduced a "Single Window" digital platform integrated with 17 government services to facilitate investor interactions.

However, implementation gaps persist. An electronic portal mandated in 2019 to track investment projects remains underutilised, and existing databases are siloed across agencies. Monitoring and evaluation processes are fragmented, with investment-related data not systematically shared between MIIT departments and UzIPA, undermining evidence-based policymaking.

The Foreign Investors Council and annual Foreign Investment Forum provide platforms for dialogue between government and investors, reflecting growing recognition of stakeholder engagement. Nevertheless, policy advocacy mechanisms remain weaker for smaller investors than for large strategic projects.

4.4. Tax Incentives and Special Regimes



Uzbekistan offers an extensive array of tax incentives for investors, including exemptions from profit tax, property tax, and customs duties for qualifying projects. These incentives are available through special economic zones, sector-specific programmes, and individual investment agreements.

However, the proliferation of incentives raises concerns about cost-effectiveness and transparency. The OECD recommends shifting from income-based to expenditure-based incentives, reducing discretion in granting tax benefits, and publishing regular tax expenditure reports to assess effectiveness. Some incentives disproportionately benefit foreign investors without clear development justifications, warranting reconsideration.

5. PERSISTENT CHALLENGES TO FDI ATTRACTION AND UTILISATION

Despite substantial progress, several challenges continue to constrain FDI inflows and limit their development impact.

5.1. Regulatory Uncertainty and Implementation Gaps

The gap between policy formulation and implementation remains a defining feature of Uzbekistan's investment climate. While laws have been modernised, their enforcement is inconsistent, and secondary legislation sometimes contradicts primary laws. The frequency of regulatory changes—businesses face an average of multiple amendments annually—creates unpredictability that discourages long-term investment commitments.

Regulatory impact assessment practices remain underdeveloped, limiting the evidence base for policy decisions. Judicial capacity to handle complex commercial disputes requires strengthening, and alternative dispute resolution mechanisms are not yet fully utilised.

5.2. State Dominance and Competition Distortions

State-owned enterprises continue to play a significant role in the economy, accounting for substantial shares of GDP and employment. Despite reform efforts, SOEs often receive preferential access to land, finance, and incentives, distorting competition and potentially crowding out private investment. The Competition Promotion and Consumer Protection Committee requires greater independence and enforcement authority to ensure a level playing field.

Privatisation of non-strategic SOEs is progressing but remains slower than initially envisioned. Accelerating this process, with transparent procedures and improved corporate governance aligned with OECD guidelines, would create new investment opportunities and reduce state dominance.

5.3. Limited SME Capacity and Linkages

The potential for FDI to generate spillover benefits through supply chain linkages, technology diffusion, and skills transfer depends critically on the absorptive capacity of domestic firms. While foreign firms source many inputs locally—suggesting supply chain linkages are fairly strong—many SMEs lack the capacity to meet the quality, scale, and reliability requirements of multinational enterprises.



Informality among SMEs remains pervasive, limiting their access to formal finance and their ability to participate in global value chains. Labour market inefficiencies, including skills mismatches and barriers to mobility, further constrain spillover potential.

5.4. Access to Finance

Private sector investment, both domestic and foreign, is hindered by underdeveloped financial markets. The banking sector remains dominated by state-owned banks with limited credit allocation to private enterprises. Domestic capital markets are nascent, restricting access to long-term finance for larger projects. These constraints affect firms of all sizes but disproportionately impact smaller investors and domestic entrepreneurs seeking to partner with foreign firms.

5.5. Skills Gaps and Labour Market Inefficiencies

Uzbekistan benefits from a young and relatively well-educated population, presenting a demographic dividend. However, skills mismatches between educational outputs and private sector needs persist. While foreign-owned firms provide training to develop worker capabilities, the broader workforce development system requires strengthening to meet the demands of a modern, diversified economy.

Labour market rigidities and information asymmetries hinder efficient matching of workers to opportunities, potentially limiting the employment impact of new investment.

6. CONCLUSION AND POLICY RECOMMENDATIONS

Uzbekistan has made remarkable progress in reforming its investment climate since 2017. The legislative framework has been modernised, institutions for investment promotion established, and administrative procedures streamlined. FDI has responded positively, with growing inflows and increasing investor interest from diversified sources.

However, the journey toward an investment climate that attracts sustainable, diversified, and development-enhancing FDI remains incomplete. Concentrated sectorally and geographically, FDI has yet to generate the broad-based spillover benefits that characterise successful investment-led development experiences elsewhere. Regulatory uncertainty, institutional fragmentation, state dominance, and limited local firm capacities constrain both the quantity and quality of investment.

Based on the analysis presented, the following policy recommendations emerge:

First, enhance regulatory predictability and implementation quality. This requires reducing the frequency of legislative changes, minimising reliance on secondary legislation, strengthening regulatory impact assessment, and building judicial capacity for commercial dispute resolution.

Second, clarify and strengthen institutional roles. Restructuring the relationship between MIIT and UzIPA, with clear delineation of strategic versus operational functions, would improve effectiveness. UzIPA requires adequate resources to fulfil its mandate, particularly in investor aftercare and policy advocacy for smaller investors.

Third, accelerate state-owned enterprise reform. Privatisation of non-strategic SOEs should proceed transparently, with improved corporate governance and elimination of preferential treatment that distorts competition.



Fourth, develop SME capabilities to enhance FDI spillovers. Comprehensive linkage programmes connecting multinational enterprises with local suppliers, supported by supplier databases and capacity-building initiatives, would facilitate technology transfer and local value addition.

Fifth, rationalise and increase transparency of tax incentives. Shifting toward expenditure-based incentives, reducing discretion, and publishing regular tax expenditure reports would improve cost-effectiveness and align incentives with development objectives.

Sixth, strengthen the financial sector and workforce development. Deepening capital markets, improving access to finance for private enterprises, and aligning skills development with investor needs would address foundational constraints to investment.

The path forward requires sustained political commitment, improved inter-agency coordination, and continued dialogue with investors and other stakeholders. If successfully navigated, Uzbekistan has the potential not only to attract greater FDI but to leverage it as a transformative force for inclusive and sustainable development.

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