INTEGRATION OF UZBEKISTAN SECURITIES MARKET INTO FOREIGN CAPITAL MARKETS

Olimjon Alimov
Researcher, Department of Corporate Finance and Securities,
Tashkent Financial Institute, Tashkent, Uzbekistan. E-mail: alim.d.alimov@gmail.com
https://orcid.org/: 0000-0001-6133-2349

JEL Classification: *D4,D40*

Abstract. *The article presents the main directions of Uzbekistan securities market's transformation at a new stage of economic reforms in 2015-2021. Local securities market infrastructure remains obsolete, financial instruments are limited, there are no effective mechanisms to stimulate market institutions, as well as passive integration of the local market into foreign capital markets, low efficiency of government regulation and investor protection remains uncertain. The key achievements in the development of securities market, which served to increase the capitalization of listed companies, and the turnover of corporate securities, are highlighted. The impact of the securities market on economic growth was assessed, which indicates that in the early stages of development, the securities market has an "explosive" effect, increasing the country's macroeconomic competitiveness for more effective integration into foreign capital markets. Measures are presented to create conditions for further integration of the local securities market into foreign capital markets. Active steps are being taken to introduce modern methods and technologies into stock exchange activities, initiatives have been launched to update legislation framework regulating activities in the capital market, and extensive programs are being conducted on the way of privatization of state assets. Market institutions work on the perfection of securities trading rules, introducing new mechanisms and technologies such as the calculation of quotation (pricing) of securities or determining the price of shares at the first stage of the REPO transaction in the trading system. In conclusion, there are given the measures and recommendations necessary for the accelerated development of the market, creation of favorable conditions for investors, infrastructural transformations, withdrawal of national companies to international capital markets are given.*

Key words. *capital market, corporate securities, economic growth, international financial system, stock exchange, securities trading*

Introduction. The economic theory shows that the global integration of capital markets provides important benefits for both, the country and the private sector. Cross-border investments help companies raise more capital at a lower cost, allowing investors to diversify their portfolios and earn higher returns than in local markets (Grauer, Litzenberger, Stehle, 1976; Errunza, Losq, 1985). At the same time, a positively functioning securities market affects the rate of economic growth, allowing companies to effectively mobilize capital for development and diversification of risks when financing capital-intensive projects (Alimov, Mukhamedov, 2021). The case for countries with a developed financial sector that experience faster economic growth is widely accepted in the theoretical literature and demonstrated by academic researchers (Karolyi, 2006; Bencivenga, Smith, 1991). The theoretical foundations of the relationship between financial depth and economic growth can be traced back to the work of Schumpeter (1934), McKinnon (1973), and Shaw (1973). The general argument is that a developed financial system reduces information asymmetries and transaction costs, leading to better resource allocation, risk diversification, increased productivity, and therefore stimulates economic growth (Boyd, Prescott, 1986). In turn, economic growth allows the local securities market to integrate into foreign capital markets. Two main channels have been identified through which the financial sector can influence economic growth. This is due to the development of the securities market and the banking sector (Beck, Levine, 2004; Adusei, 2013). Unlike short-term lending by banks, securities markets provide long-term capital in primary markets, increase the efficiency of capital allocation for profitable projects, provide equity holders with the opportunity to sell their stake in companies in the secondary market, and the growth and development of the securities market reflect the growth of investor confidence in work of the local economy.

The development of the securities market over the past 5 years has been a priority in reforming the economy of Uzbekistan. At first glance, there are necessary prerequisites and conditions for its successful development: a regulatory and legal foundation has been created, measures have been taken to ensure market transparency and improve the corporate governance system in companies, and a market infrastructure has been formed. However, an analysis of the indicators of the securities market of Uzbekistan over the past ten years does not give grounds for a positive assessment of its condition. The depth of the securities market can be characterized by such indicators as the number of active players in the market, the volume of capitalization of listed companies, shares and debt securities in circulation, or the entire volume of the securities market as a percentage of GDP.

Materials and methods. Considering the integration of the securities market into foreign capital markets through the prism of economic growth, scientists in their studies on this hypothesis through econometric analysis noted that institutional indicators are significant in empirical models of economic growth (DeLong, 1993). Subsequent work confirms the positive correlation between economic development and financial market indicators when using a 20–30-year period. The emergence of accessible macroeconomic statistics for most developing countries in the 2000s. made it possible to revise the works of 20 years ago and move the topic of discussion to a slightly different plane. These issues have become relevant in works that point to the non-linear nature of the relationship between financial markets and GDP growth rates. Western economists in their studies confirm the relationship between the development of the securities market and the dynamics of economic growth through stable investments (Barro, 1996). Econometric estimates of economic growth models with the inclusion of variables reflecting the "depth" of the securities market (the ratio of market capitalization, savings, and investment in the financial sector to real GDP) indicate the statistical consistency of these variables. In general, these regressions can be represented as follows:

$$growth_i = \alpha_0 + \alpha * F_i + \beta * X_i + \varepsilon_i ,$$

where α_0, α, β are coefficients, F_i is an indicator of the development of the financial market of country i (the share of market capitalization in % of GDP), X_i are the values of auxiliary variables (the level of investment, inflation rates, protection of private property, etc.) for country i, ε_i – random regression error. The positive impact of the financial market, including the stock market, on the country's economic growth can be said if the coefficient α with the variable F_i is positive and statically significant.

The resulting regression model looks like:

$$growth_i = 7.81 + 0.005 * F_i - \beta X + \varepsilon_i.$$

This means that in the long term (1990–2020) the growth of capitalization of the securities market by 10 p.p. was associated on average with GDP growth by 0.4 p.p. In addition, a number of empirical works note the non-linear contribution of the development of the securities market to economic growth in the short term. To test this hypothesis, a simple three-way regression of the species over the period 2000–2020 was evaluated:

$$growth_i = 4.967 - 0.0463 * F_i + 0.0265 * F_i^2 + e_i$$

$$\frac{\Delta growth}{\Delta mcap} = -0.0463 + 2 * 0.0265 * F_i = 0$$

$$F_i = 88\%.$$

According to the calculations obtained, on average, the growth of the market capitalization of listed companies up to 88% is accompanied by GDP growth rates, in countries where this indicator exceeded the threshold value, the growth of the securities market reduced the GDP growth rates (base effect).

Results

Western economists (Levine, 2004) in their studies confirm the relationship between the development of the securities market and the dynamics of economic growth through stable investments. For example, the share of market capitalization of listed companies to GDP in Uzbekistan for 2021 is 9.1%. By comparison, this figure only in Kazakhstan and Russia amounted to 26.4% and 46.7%, respectively, not to mention countries with similar economic development (Fig. 1).

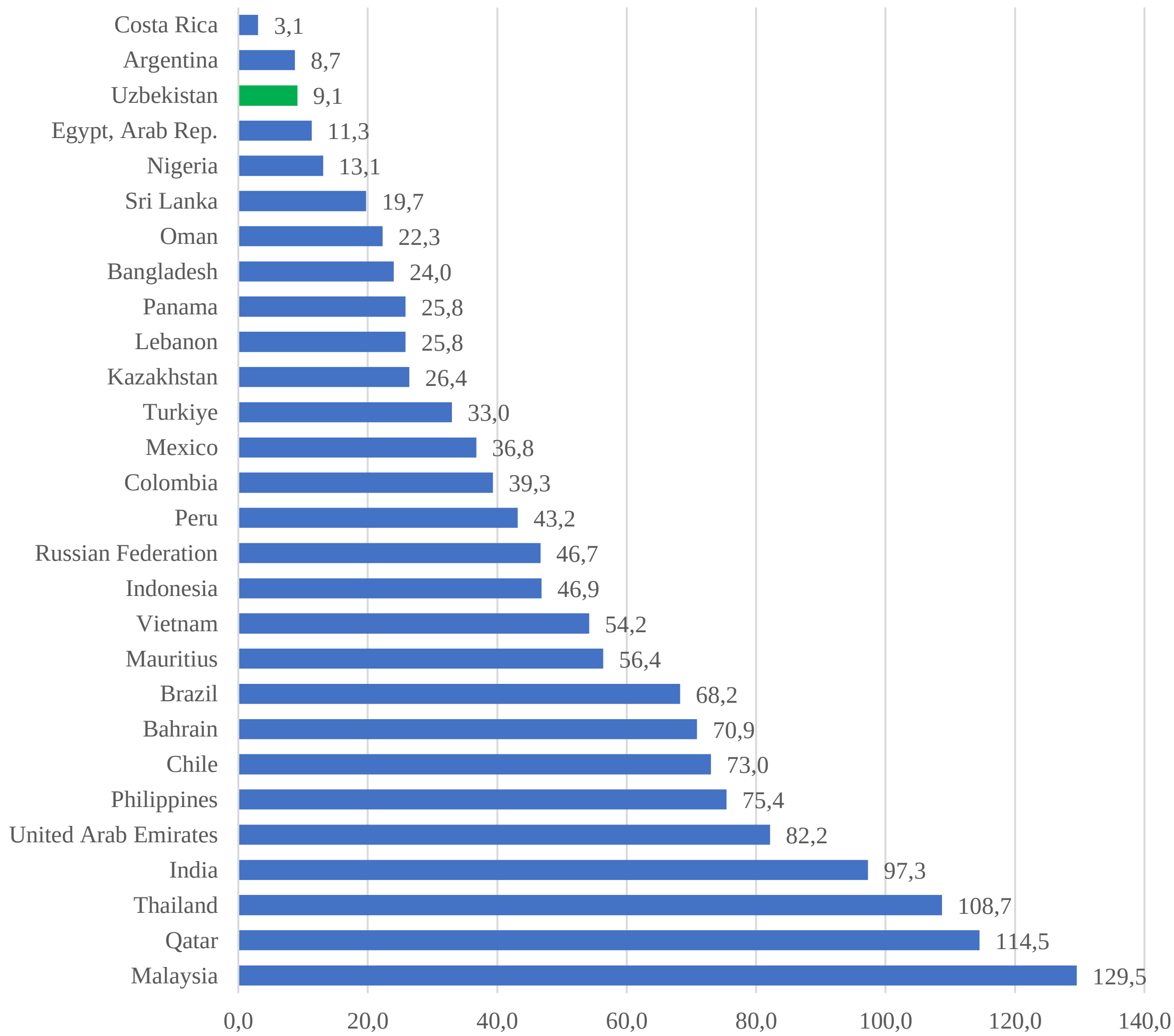

Figure 1. Ratio of market capitalization of listed companies to GDP, 2021.

Source: Compiled by the author based on data from the World Bank and the State Statistics Committee of the Republic of Uzbekistan.

The experience of developing countries shows that in the long run, a stock market growth of 1% is associated with GDP growth of 0.3 percentage points. At the same time, the statistical analysis carried out showed that the development of the securities market of Uzbekistan is a statistically insignificant factor in economic growth in the 2000s.

The construction of scatter charts and the corresponding one-factor regressions for the development of the securities market and the level of the informal economy showed that the growth of the shadow economy by 1% leads to a decrease in the development of the securities market by 3% (Fig. 2). At the same time, the shadow economy explains more than 40% of the cross-country variation in the levels of development of the securities market.

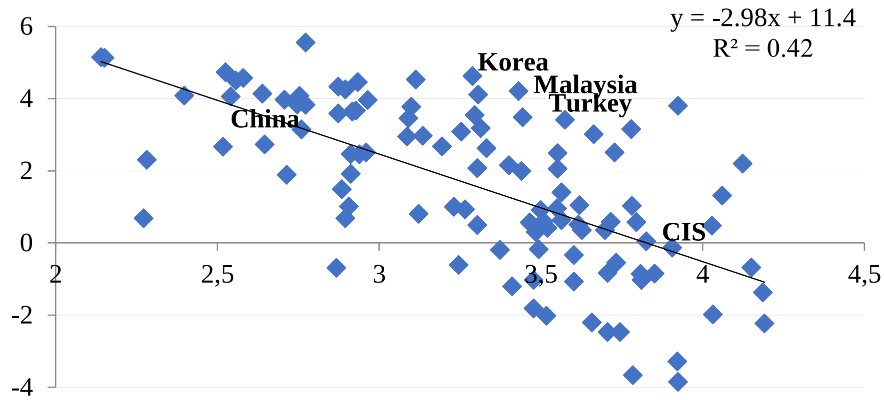

Figure 2. Scatter diagram of the level of the informal economy and the development of the securities market (for comparability of the scales, the axes are taken logarithmically).

Source: Compiled by the author based on World Bank data.

At the same time, one of the main shortcomings of the local securities market on the way to development and fundamental reform is the immobility of most of the shares, as a result of the lack of liquidity in the market. The main reason for this situation is the dominant role of the state as a shareholder in the market. For example, as of 2021, out of the total nominal value of shares in the amount of 153.1 trillion soums, the state’s share in the authorized capital of 234 JSCs is 125.3 trillion soums or 81.9%. At the same time, since 2015, there has been a steady upward trend (Fig. 3).

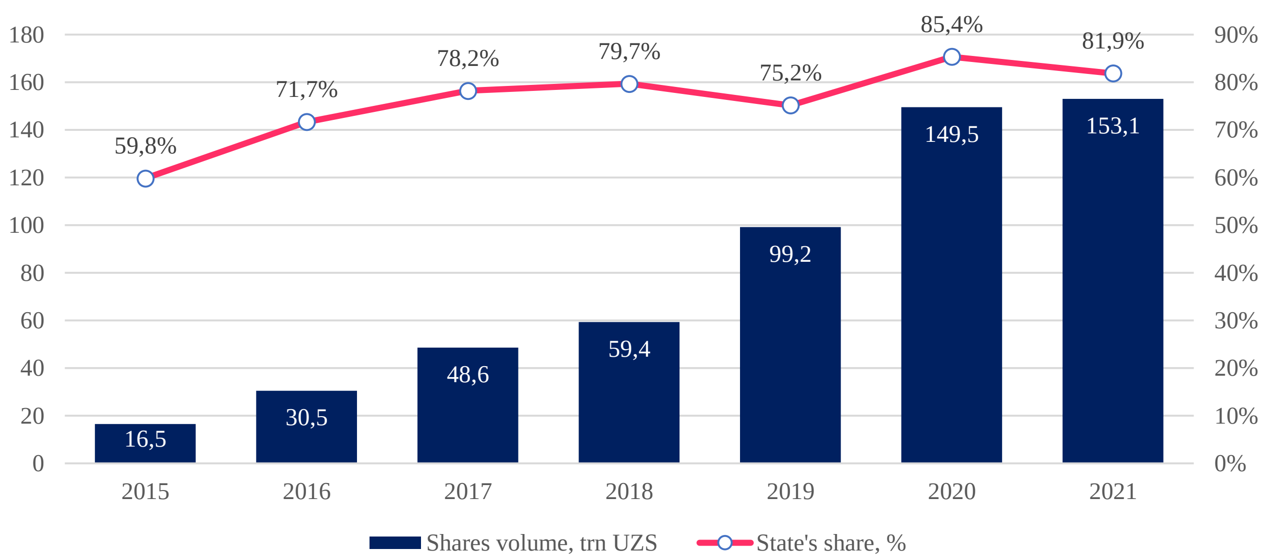

Figure 3. Dynamics of the volume of shares in circulation and the share of the state in the structure of ownership of company shares, 2015-2021.

Source: Compiled by the author based on data from the Central Securities Depositary of the Republic of Uzbekistan.

These indicators do not take into account the shares owned by the state through business entities and organizations with a state share on the basis of trust management. The presence of the state as a shareholder in the authorized capital of the company imposes a special procedure for making managerial decisions, including the sale of assets (shares) on its balance sheet, which is one of the main reasons for their passivity in the capital market.

In addition, there is a decrease in the number of JSC while increasing the total volume of stock issues. Thus, since 2012, the number of JSC has decreased more than twofold, with the total volume of issues increasing 16.8 times. In turn, the restriction on the sale of shares in the secondary market outside the organized trading platforms established by the Uzbek legislation did not lead to a significant increase in the secondary market indicators, moreover negatively affects the liquidity of the shares, limiting their fundamental property as an object of sale.

The organized securities market is represented by two participants - the RSE "Tashkent" and the over-the-counter system of electronic trading in securities "Elsis-Savdo". For the period from 2015–2020 the volume of trading on the organized market was accompanied by characteristic fluctuations due to the reform of the entire capital market. At the same time, the volumes of the exchange market average 92% of the entire organized market (Fig. 4).

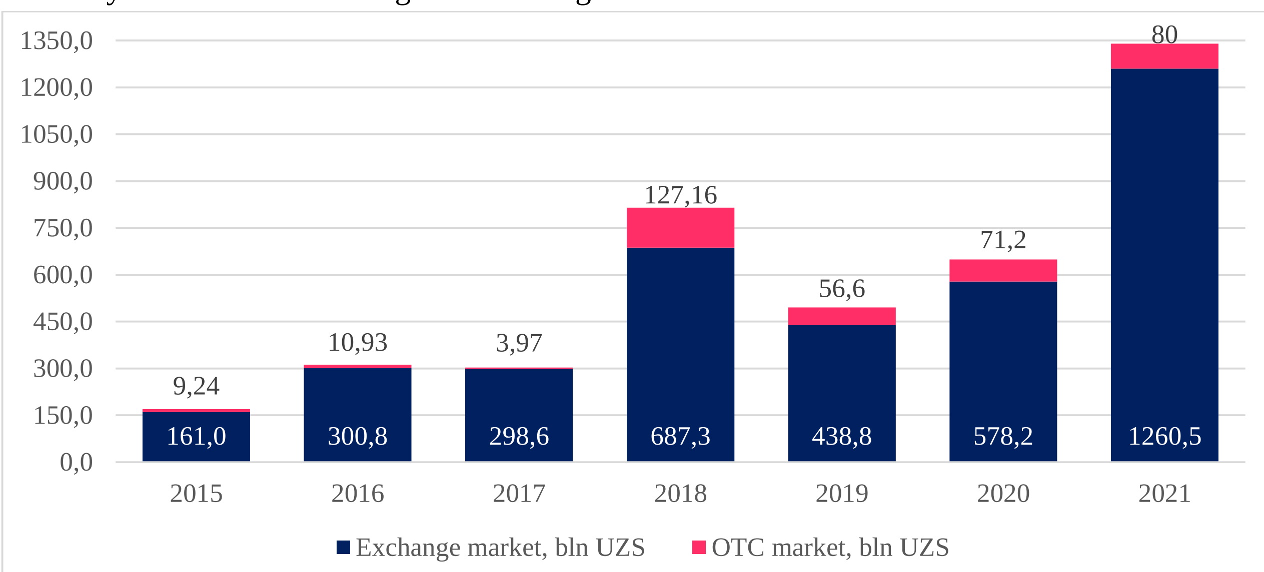

Figure 4. Dynamics of the volume of the organized securities market, 2015-2021

Source: Compiled by the author based on data from the RSE "Tashkent", ESWT "Elsis-Savdo".

RSE «Tashkent» works on the perfection of securities trading rules, introducing new mechanisms and technologies. Thus, from April 1, 2022, a new order of calculation of quotation (pricing) of securities is determined. The quotation of the shares included in the exchange list is carried out depending on the level of their liquidity and is updated monthly. Besides since April 26, 2022, the order of determining the price of shares at the first stage of the repurchase transaction in the trading system was introduced. The «Haircut» ratio of listed companies is set at 20% for listed shares of the «Premium» category, for average liquid securities at 30%, and for other shares included in the «Standard» category the ratio remains unchanged (at 50%).

Discussion

According to the results of the study of capital markets in emerging countries of the world, the factors influencing the development of capital markets on the way to integration into foreign capital markets can be conditionally divided into two groups: ones as part of a general favorable environment; and others directly related to the specific functions of capital markets. For the successful development of a viable capital market, it is recommended:

- liberalization (ensuring autonomy) of capital markets;
- strengthening the legal and judicial systems for protecting investors;
- increasing the independence and effectiveness of regulation;
- increasing the depth and diversity of the local institutional investor base;
- wide and bidirectional opening of capital markets;
- strengthening market ecosystems through the development of deeply complementary markets for derivatives, repo transactions and securities lending (Bank for International Settlements, 2019).

Some of the main factors for the successful development of capital markets in emerging countries are:

1. Creation of additional investment opportunities by encouraging broader issuer participation through:

   a. optimized issue processes and procedures;
   b. economic policies that encourage issuers to enter the capital markets;

2. Expand the investor base by improving the value proposition for investors through:

   c. reforms that encourage both foreign and domestic investment;
   d. tax regimes consistent with financial development goals;
   e. strengthened regulatory frameworks that protect investors;
   f. strengthening the corporate governance system.

3. Improvement of market access and efficiency by:

   g. data collection and dissemination;
   h. development and growth of standard types of products (for example, repurchase agreements, securities lending and derivative financial instruments) (World Economic Forum & Oliver Wyman, 2016).

Conclusion

In the development of local capital markets, it is recommended to be guided by the following conclusions:

i. the capital market development depends on prudent macroeconomic policies and a legal environment that protects property rights;
ii. the development of the capital market takes time and the right sequence of decision-making, as some markets require a more developed financial infrastructure and stronger legal protection for development;

iii. iii. capital market development can be facilitated by policies that increase the size of the market, including pension reform, financial liberalization, and tax reforms;

iv. iv. rules that promote disclosure of information, standardization of securities and prevention of violations when concluding transactions with securities will contribute to the development of an effective primary and secondary securities market (Laeven, 2014).

Given the right conditions, a country can create a local securities market that efficiently allocates capital to support economic growth and further integration into foreign capital markets.

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