



Quote of the month

“The national economy has no future without digital economy”

President of Uzbekistan on the implementation of digital economy and e-government. September 22. [Link](#).



Source: Russian Presidential Press and Information Service. [Link](#).

Figures & data of September

4.8-5%

Expected growth rate for 2021 in Uzbekistan, according to the World Bank, despite the COVID 19. One of the best rates in the region. [Link](#).

5,000

The number of outdated standards Uzbekistan is removing to be in line with the EU and the EEU product's standards requirements. [Link](#).

3.8%

The performance ration of a major solar energy project in Kazakhstan which is higher than initial expectations of performance. [Link](#).

11.4%

Turkey's official inflation rate last June but in a recent survey around one-third of respondents said the real inflation rate was above 30%. [Link](#).

China and Russia are unmissable economic partners for the economies of Central Asian and claim to have a mutually beneficial partnership. But for how long?

In most people's mind, both countries have tacitly agreed on complementary roles in Central Asia. China provides the funds for economic development and Russia maintains a favorable political and military climate. However, Beijing expanded its influence in the region into other fields making Russia think the tacit agreement changed without prior notice.

Both countries looked for opportunities for regional economic cooperation, but it did not create the expected economic benefits and opportunities since none of the two partners are really willing to concede too much of their own projects.

Russia is ready to cooperate to Chinese Belt & Road initiative in Central Asia and sees opportunities to create and develop infrastructures that would, with Russia alone, be much more limited.

However, it does not want it to surpass the EAEU which is one of its primary tools for regional cooperation. China perfectly understood this fear and refused to take up even one out of the 40 transportation projects put forward by the EAEU.

The solution could come from a third player: India whose membership of the Shanghai Cooperation Organization has been pushed by Russia.

A stronger India will balance China's influence while being constrained to cooperate with Russia since the International North-South Transport Corridor, bypassing Pakistan and China, requires Russia.

The Chabahar port project, in Iran, and India's accession to the Ashgabat Agreement are two key achievements to be monitored closely. The role of Iran, now closer to China, will be decisive.



News from the Centre's press reviews present a brief overview of the main points of interest that occurred during the previous month in the CAME region (Central Asia and Middle East). It covers, among others, tax & law, investments and trade, as well as business life at large.

- ❖ **CENTRAL ASIA, CAUCASUS AND RUSSIAN WORLD** – Forbes noticed that, in a few short years, **Uzbekistan** has come charging out of its long sleep to set an example to all the 'Stans roundabout on how to usher in a new era, returning to its historical role as the hub of the Silk Road ([Forbes 30.09](#)). For the record, in 2019, The Economist named Uzbekistan country of the year, one that “*has travelled furthest*” in its reforms and improvements on all fronts, adding that it needed to keep improving. Time has proved The Economist to be right!

Uzbekistan is selling part of its gold reserves to save the economy becoming one of the largest gold exporters. On September 21, the State Statistics Committee reported that the country exported US\$5.8 billion worth of gold in the first eight months of 2020. The sale of precious metals accounted for half of the export proceeds. To compare, Uzbekistan exported \$ 4.9 billion worth of gold for the whole of 2019 ([Eurasianet 23.09](#)).

The Transportation-Logistics Centre of **Turkmenistan** reported that the longest-ever container train would arrive in that country two days later from China, after a journey of only two weeks making it the most timely and economically effective path for Chinese trade with Central Asia, the Caspian and even Europe ([Turkmenportal 09.09](#)). Russian officials stress that its activities only became possible thanks to Moscow's North-South Transportation Corridor Project. Nonetheless, China's regional role is different and larger: it is sending consumer goods and other finished products that are more likely to find buyers in these countries than Russian raw materials, like oil and natural gas. Moreover, Beijing offers these countries the possibility of shipping some of their industrial production to the Chinese market, which is far larger and more interested in such purchases than **Russia's**. ([Xinhua—Russian service 10.09](#), [Info24.ru 11.09](#)). (See also [Jamestown 24.09](#)).

Kazakhstan country took over the chairmanship of the Conference on Interaction and Confidence Building Measures in Asia from **Tajikistan** will continue to promote further cooperation between members ([Russia News 25.09](#)). **Kazakhstan** and **Turkmenistan** discussed the initiation of a special customs zone on the border and evoked further cooperation in trade and energy, economy and investment, transit transport, and agriculture ([primeminister.kz 17.09](#)). Tajikistan is eager to increase the economic cooperation with neighbouring countries. A similar discussion took place with Uzbekistan about diversification of the trade structure and overcoming technical barriers to trade, the opening of trading houses, representative offices, and branches, better use of investment cooperation potential ([Sputnik News 29.09](#)).

- ❖ **CHINA AND THE BELT AND ROAD INITIATIVE** – A 25 years old project of a railway between **China**, **Kyrgyzstan** and **Uzbekistan** is under the light again since **Russia** could be an active player to settle the project. The project has been on hold due to the Kyrgyz attitude (difficulty to finance, few local benefits, technical challenges). This attitude could evolve in the near future if certain concessions are granted by the other players, especially China which has a short term (access to Uzbek oil field of Mingboulak) and long-term goals (possibility of extension toward Afghanistan, Iran, Turkey then Europe). However, Russia has no direct interest in this project and the conditions of its participation should be monitored closely ([Novastan 09.10](#)).

Recently **China** is pushing **Pakistan** to open its five key border crossings with **Afghanistan** to allow bilateral and transit trade and the resumption of Afghan exports to **India**. Afghanistan is a landlocked country and relies on Pakistani land routes and seaports to conduct international trade. The two countries share 18 crossing points, of which the most commonly used are Torkham in Pakistan's northwest and Chaman in its southwest ([Asia Nikkei 01.09](#)).

- ❖ **IRAN, TURKEY AND MIDDLE EAST** –Turkmenistan currently exports its natural gas to only one buyer, China, and badly needs to diversify its export destinations. **Iran** and **Turkmenistan** had a dispute over gas trades, which was addressed by the International Court of Arbitration earlier this year. Iran expressed its interest to resume the import of Turkmenistan's gas ([Mehr News 01.09](#)). The Turkish lira found another all-time low against the dollar In September sinking to 7.8362 ([BNE 28.09](#)). This situation attracts foreign investors willing to have a cheap investment in Turkish banks but the country's situation is still very instable and investors might have surprises ([BNE 27.09](#)).





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- ❖ **COMPLIANCE, SANCTIONS & BUSINESS LAW** – The Trump administration has imposed sanctions on 18 "major" **Iranian** banks in one of the most extensive such moves by Washington against Tehran in months. The order will also penalize non-Iranian institutions trading with them, effectively cutting the banks off from the international financial system ([BBC News 09.10](#)). The National Bank (**Uzbekistan**) will connect to the financial messaging system of the Bank of Russia. SPFS is a specialized channel for transmitting electronic messages on financial transactions analogue to the SWIFT system but without its exposure to US secondary sanctions ([EUROUZ 09.20](#)).
 - ❖ **INVESTMENTS, TRADE & PPP** – President of Tatarstan (**Russia**) launched the implementation in **Kazakhstan** of three joint projects in the automotive industry pertaining to cast iron, components for the bridges of trucks and a tire production facility. The implementation of the projects will introduce Kazakhstan into the global technological chain of suppliers of the largest manufacturer of trucks in the CIS market ([Times of CA 29.09](#)). Uzcharmsanoat Association has concluded a number of agreements with Nike and Adidas. The production of sports shoes will be launched in **Uzbekistan**. It is planned to produce 3 million pairs of sneakers under the world-famous brand at the SinoInternational JV LLC plant through outsourcing contracts. 15 new export markets are expected to open over the next three to five years, mainly in Europe but also South-East Asia ([EUROUZ 09.20](#)).
 - ❖ **BANKING, TAX & FINANCE** – Kazakhstan is on track for \$700M crypto mining investment goal and claims that there are already preliminary agreements on attracting more than \$700 investment for cryptocurrency mining. **Kazakhstan** had established cryptocurrency tax regulations in 2019 which rendered earnings through crypto mining tax-free as long as the coins were not converted to fiat money ([Coin Telegraph 02.09](#)).
- Uzbekistan** and **Germany** agreed on the creation of a local bureau of the Credit Institute for Economic Recovery in Tashkent. The KfW Development Bank, a member of the KfW Bankengruppe financial group, is responsible for financial cooperation with partner countries. On behalf of the Federal Government, the KfW Development Bank finances investments and related advisory services and skills development activities ([Uz Daily 02.10](#)). The Uzbek Capital Market Development Agency held the first bilateral negotiations with the **Dubai** International Financial Center (DIFC). The parties agreed to establish partnerships in terms of effective development and modernization of the regulatory framework of Uzbekistan, which will allow companies and citizens of Uzbekistan to gain access to world financial markets through the infrastructure of the DIFC ([EUROUZ 09.20](#)). Two recent **Uzbekistan** president's Decrees, adopted on September 15, approved two conventions of Uzbekistan with **Japan** and **Korea** pertaining to double taxation with respect to income taxes and the prevention of tax evasion and avoidance ([Taxnotes 18.09](#)).
- ❖ **ENERGY, OIL & GAS, RENEWABLE** – A solar power plant, financed by German investors, with a capacity of 26 MW (62 thousand photovoltaic panels) was put into operation in **Kazakhstan** ([Kazakh Invest 02.09](#)). This is not an isolated project since The European Bank for Reconstruction and Development is organising a new financing for the construction of a 76MW solar plant in the same region of Kazakhstan ([Times of CA 19.09](#)). Kazakhstan is a leader in the development of renewable energy in Central Asia, with a total installed solar capacity of 216MW. Renewable Energy projects attract a rising number of European companies.

An agreement was signed with the **Japan** International Development Agency for the implementation of a project for the construction of a third combined cycle gas turbine plant in **Uzbekistan**. The Agency will allocate 128.246 million yen (USD 1.18 billion) as a loan for 30 years ([Uz Daily 11.09](#)). Meanwhile, Uzbekistan's Ministry of Energy said that a 20-year loan agreement, worth €55.8 million, has been signed with the **French** Development Agency (FDA). The loan facility will finance a series of projects in Uzbekistan's hydropower sector. The projects are part of an ongoing initiative by JSC Uzbekhydroenergo called "Project Factory" promoting the development and implementation of new investment projects based on modern technologies. The total of 23 projects with projected capacity of 907.5 MW, worth \$1.37 billion are currently underway ([Times of CA 01.09](#)).





INTERVIEW

M. Kiyan ZANDIYEH

Chief investment Officer and Portfolio manager of the investment fund Sturgeon Capital

Sturgeon Capital is a privately owned investment boutique specialising in investment opportunities in Central Asia region with a focus on Uzbekistan. Kiyan gave us the opportunity to explore several topics pertaining to frontier markets, opportunities in Central Asia and Uzbekistan, energy and financing sectors. Despite remaining political and currency risk in the region, the performance of the funds makes them able to mitigate the investors' risks provided that investments projects are carefully selected in promising sectors.

Thanks for taking time for this interview. Could you briefly present Sturgeon Capital?

We are an investment firm focussed on investing and building in technology and technology enabled businesses in frontier countries that are yet to experience broad based technological evolution.

We define **frontier countries** as those that have for an extended period of time had little in the way of private sector participation in their economy. This lack of private capital - which is usually well incentivised to capitalise on opportunities – means that these countries present an abundance of opportunities for investors to capitalise on.

We typically get interested in a country, where there is some sort of catalyst where private sector participation in a country goes up and by virtue of that foreign investment.

When observing these countries, **they all have high levels of internet and smartphone penetration but haven't yet seen technology enabled business models being built, that we have become accustomed to in the developed world.** Our favourite business models are those that have proven to be successful in other parts of the world and viewed through the lens of Maslow's hierarchy of needs provide products and services that address the basic needs of the general population.

Ultimately, they are monetising the efficiency gains they introduce. When finding these businesses, our job is to provide capital and work actively with the businesses to scale and be leaders in their respective business in their countries and regions of operations. for them to realise their full potential.

How to appreciate political and currency risks which are more likely in these markets?

Starting with political risk, one of the reasons we focus on technology-based businesses is that **you would find it hard to find a country that has been able (whether they've wanted to or not) to get in the way of technological progress.** Once the cat is out the bag, it's out.

'you would find it hard to find a country that has been able (whether they've wanted to or not) to get in the way of technological progress'

The second is that these businesses are primarily comprised of **intangible assets, which are operationally complex to develop and difficult to expropriate.** Historically, frontier investors have often seen political pressure, when they've invested in companies that whilst nominally cheap, operate in an area that is strategically important for a country, or potentially tread on the toes of various power centres. Investing in technology stays away from this and has another factor which is important to us – whether a business adds or takes away from the eco-system. In e-commerce for example, we're making it easier for consumers to buy a wider array of goods at cheaper prices, helping local logistics companies increase revenues and helping local offline retailers increase their sales through linking with the online platform. Here the whole eco-system wins. This is the opposite of investing in say a bottling company, where the main way to generate returns is by taking market share away from an incumbent and increasing the prices of the products, which is inflationary to the consumer.



Source: Courtesy of Kiyân Zandiyeh

As it relates to currency, each country has their own dynamics. ***We like countries like Uzbekistan which have natural current account surplus's and low debt levels such that structurally the country is less vulnerable to currency shocks.*** Separately we our aiming to invest in businesses that have very high growth rates such that the net return to us as in investor minus any currency weakening (which we factor in) is still high

Isn't possible to mitigate these risks with the performance of the funds?

Our return target for the fund is quite clear. To return 5x in USD in 5 years. From an investing perspective this means investing in businesses that are very scalable, have near zero marginal costs to growing and have clear product market fit. In e-commerce for example we're seeing 50% month on month growth. Whilst growth rates at such levels won't sustain, even a fraction of it compounded over five years outweighs currency risks.

Other countries we've invested in have seen severe currency shocks (over 80% weakening), and the environment has played in the favour of technology companies, providing their a product or service that is more efficient and cheaper than the offline alternative.

In such scenarios the cost of operating and market share go down, in line with the currency, yet your customer adoption goes up significantly, which again makes up for currency losses.

Ultimately, our investment framework has been borne out of investing in countries that are difficult to operate in, and so resiliency as a concept for the companies we invest in is very important.

Why is Sturgeon Capital focused on Uzbekistan and how is the situation different from the economic opening which occurred previously in other neighbouring countries ?

Uzbekistan is a country we've been involved in for about eight years. Within central Asia it has the largest population (35m people), 65% of which are under 35. The legacy of the Soviet Union is also a very educated population, focussed on the hard sciences. The issue was that under the previous administration the country was effectively closed off to foreign investors and so that talent didn't have fertile grounds to thrive.

Economically, the country generates revenue from diverse sources. Unlike other countries in the region, they're not reliant on oil & gas. They're largest natural resources are Gold and Uranium, which are counter cyclical assets. They also have very low levels of debt (under 30% to GDP) and high reserves (60% to GDP). So, the economy from a structural perspective has strong foundations. Separately from a GDP per capita perspective, the country currently is at \$1,500. If you compare that with Georgia with 1/5 of the population and no natural resources, it's at \$4,500. So the country is coming from a very low base, and we believe can play catch up in the years ahead.

Since the new administration came to power, they've embarked on a series of reforms, which if put into the context of any other country would be considered astounding. Ministers now are young western educated technocrats, all state assets are to be privatised, corporate tax rates have been nearly halved, and the government is moving all government infrastructure to digital means (e.g. before if it took you 20 days to register a business, today it's 20mins and all online).



So to sum up, it's a country we know well, has the positive tailwind of reforms and economic growth and a blank canvas in terms of tech enabled businesses for us to use the strong digital infrastructure (70% internet and smartphone penetration) to invest and build the leading technology businesses in the country.

We have seen a wave of promising economic reforms in Uzbekistan from February 2017. However, the financial sector is far from being updated. Do you foresee any evolution to attract foreign banks and/or foreign investments in the soon-to-be privatized Uzbek banks?

We see the opportunity for foreign banks to enter the market, and this is happening. TBC from Georgia has entered along with Halyk in Kazakhstan. This will likely continue.

With that said, what we're interested in, is being able to use non-bank technology companies to provide financial services. For example, we have a business – Billz – which provides inventory management and account management software to SME's (which represent 60% of GDP). With the data generated from the software the company can partner with banks to provide working capital loans to SME's. Similarly, with e-commerce, we have nearly a million users across the region including Uzbekistan. Here again, we can partner with banks to provide consumer loans to the platform's customers.

Frontier countries don't typically follow the route of more developed markets in the evolution of their financial industry, and China is a good example of this, where Ant Financial (Alibaba) has built one of the largest financial services businesses through their e-commerce business.

'We see the opportunity for foreign banks to enter the market, and this is happening. TBC from Georgia has entered along with Halyk in Kazakhstan. This will likely continue.'



So far, sectors like microfinancing and consumer financing are not very developed despite the growing needs from consumers and SMEs. Do investments in such markets provide enough performance to mitigate the currency risk?

We believe they do. SME's represent 60% of GDP in Uzbekistan and currently have no real access to financing. Their main source of financing is supply side financing with the costs being nearly +100%.

The issue is credit data, and being able to make an appropriate appraisal of risk, such that you can lend at more appropriate rates, whilst being profitable. Currently microfinance (MFI) businesses are small with limited balance sheets, and cater to a small group of businesses. Using the combination of digital distribution (through our software company), a team that has the track record of building successful MFI's in frontier countries, and a strong balance sheet, we're actively investing in the space to build the country's leading microfinance businesses.

We see roughly \$2bn of lending opportunity a year, and so far no one has built a business that can seriously challenge it. Similarly we're building the lending functionality in our e-commerce business, where we know we already have access to a large customer base, and with the data being generated, can overlay lending to lend to a broader pool of customers that a bank typically would, through traditional distribution mechanisms.

To go further – IFC's recent actions to increase access to finance in Uzbekistan include a \$5 million loan to DAVR BANK to expand financing for micro, small and medium enterprises to help them grow and create local jobs in the country. [Link](#).

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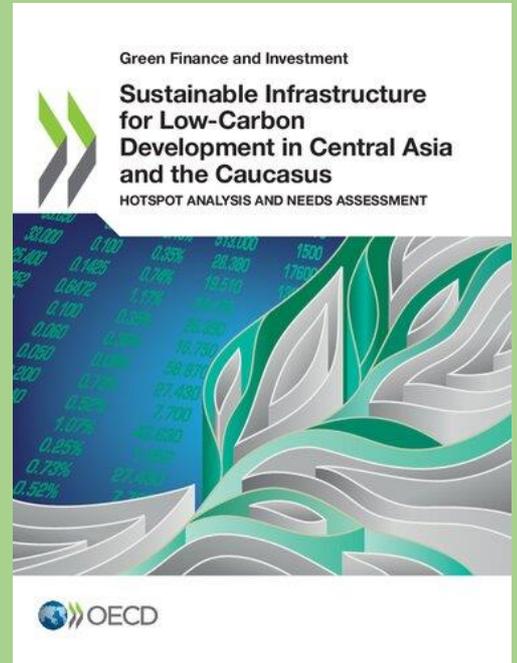
PUBLICATION REVIEW

Sustainable Infrastructure for Low-Carbon Development in Central Asia

Most economies of Central Asia and Caucasus are looking at diversifying their economies and integrating to global value chains to protect themselves from commodity price volatility but their existing infrastructure underperforms after decades of underinvestment.

The Asian Development Bank estimates investment needs of around USD 33 billion annually until 2030. Transportation infrastructure are priority. There is a variety of initiatives and plans for enhancing connectivity and integration across Europe and Asia which represent an opportunity to promote sustainable development goals or could lock in carbon-intensive technology and unsustainable development patterns for decades to come.

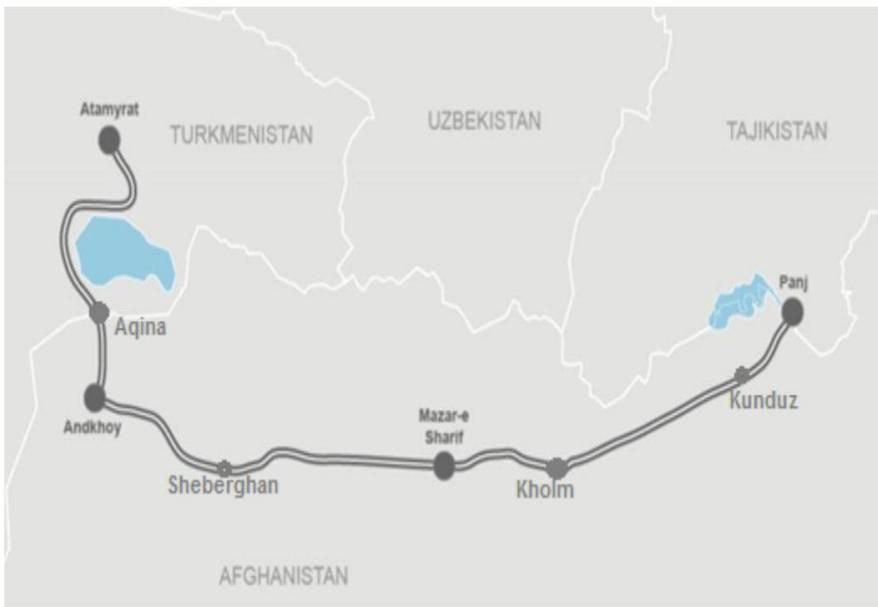
So far, these objectives are not really taken into account. The article suggests a few propositions of improvement in order to develop low-emission development strategies and evaluate current projects and strategies



OECD (2019), *Sustainable Infrastructure for Low-Carbon Development in Central Asia and the Caucasus: Hotspot Analysis and Needs Assessment*, Green Finance and Investment, OECD Publishing, Paris, <https://doi.org/10.1787/d1aa6ae9-en>.

MAP OR GRAPHIC OF THE MONTH

The TAT railway project: A road that was never built



Source: CABAR, *TAT Railway Project: A Road That Was Never Built*, 15.09.20. [Link](#)

The fate of the Turkmenistan – Afghanistan – Tajikistan railway project is still unclear despite that its importance is strategic and could compete the Chinese initiatives in the region, including by bypassing Uzbekistan.

Tashkent is striving for regional leadership and not delighted by this project of an alternative road. It is very likely than Tashkent will deepen its relations with Dushanbe offering the cheapest option for routes (auto, railways or flights) for anyone interested in the TAT road.

Tashkent will not have to fight a lot since the COVID keep all borders closed and international financial institutions are less likely to finance (see situation in Afghanistan). They can now hide behind the COVID.

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