REDUCING THE STATE'S SHARE IN THE BANKING SECTOR AND STRENGTHENING COMPETITION

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Abstract: The article analyzes the economic consequences of state ownership in the banking sector of a market economy, the importance of competition among banks, and the process of reforming and privatizing state-owned banks in Uzbekistan. Based on official data for 2019–2026, the share of state banks in assets, the costs of their recapitalization, the privatization strategy and timeline, and the entry of digital banks into the market are examined. Proposals for strengthening competition and accelerating privatization in the banking sector are developed.

Key words: market economy, banking system, state-owned banks, privatization, competition, digital banks, credit resources, financial stability.

INTRODUCTION

Banks occupy a special place in a market economy. They transform short-term savings into long-term loans, evaluate the creditworthiness of borrowers and thereby decide which firms and projects receive financing. The efficiency with which the banking system allocates credit therefore largely determines the productivity of investment and the pace of economic growth [6]. When banks operate on commercial principles and compete with each other, credit flows to the most promising borrowers; when banks are owned by the state and follow administrative directives, credit is often allocated on the basis of political priorities, which can lead to inefficient investment and the accumulation of bad loans.

For a long time, the banking system of Uzbekistan was dominated by state-owned banks, which financed state programs and large state enterprises, often on preferential terms. According to the International Monetary Fund, banks with state participation held about 84% of financial sector assets in 2019 [8]. Such a structure limited competition, reduced the efficiency of credit allocation and created significant fiscal costs: between 2017 and 2023, recapitalizations of state-owned banks from public funds ranged from 0.4% to 2.0% of GDP per year, amounting cumulatively to about USD 5.8 billion, or 5% of annual GDP [7].

Since 2019, Uzbekistan has been implementing a strategy to reform the banking sector, aimed at reducing the state's share, privatizing a number of state banks and increasing competition. By 2025, the share of state banks in sector assets had fallen to about 65–67% [7; 8], and the updated strategy envisages reducing the number of state banks from nine to four and their share of banking assets to 55% by 2030 [9]. At the same time, privatization has proceeded more slowly than planned, while new private digital banks have rapidly gained market share.

The purpose of this article is to analyze the process of reducing the state's share in the banking sector of Uzbekistan and its impact on competition, as well as to develop proposals for accelerating reforms. The objectives of the research are: to summarize theoretical approaches to state ownership of banks; to assess the dynamics of the state's share and the fiscal costs of state banks; to analyze the privatization strategy and the reasons for its delays; and to evaluate the role of digital banks in increasing competition.

LITERATURE REVIEW

The question of whether governments should own banks has been the subject of extensive theoretical and empirical research. Two main approaches can be distinguished. The "development" view holds that state banks can finance socially important projects that private banks ignore because of market failures. The "political" view, in contrast, argues that state ownership allows politicians to direct credit to supporters and inefficient enterprises.

R. La Porta, F. Lopez-de-Silanes and A. Shleifer, using data for 92 countries, found that government ownership of banks was widespread worldwide and that higher state ownership in 1970 was associated with slower subsequent financial development and lower growth of per capita income and productivity [1]. These results support the political view and suggest that state ownership of banks hinders, rather than promotes, economic development.

S. Claessens and L. Laeven, analyzing the banking systems of 50 countries, showed that the degree of competition in banking depends less on market concentration than on contestability — the absence of barriers to entry for new banks, including foreign ones, and the absence of restrictions on bank activities [2]. This conclusion is important for Uzbekistan: competition can be strengthened not only by privatizing state banks but also by facilitating the entry of new players, including digital banks.

J. Kornai's concept of the "soft budget constraint" explains why state banks tend to accumulate bad loans: both the banks and their borrowers expect that losses will be covered by the state, which weakens financial discipline [3]. The repeated recapitalization of state banks in many transition economies is a direct manifestation of this phenomenon. W. Megginson and J. Netter, summarizing the empirical evidence on privatization, show that privatized firms, including banks, generally become more profitable and efficient, especially when privatization is accompanied by the entry of experienced strategic investors [5].

Among Uzbek researchers, M. Qulmetov measured competition in the commercial banking sector of Uzbekistan for 2020–2024 using the Herfindahl–Hirschman index and the CR4 concentration ratio, and found that competition is at a moderately high level, with digital technologies and fintech innovations being the main factor accelerating it [4]. Former Deputy Minister of Finance O. Isoqov, discussing the delays in privatization, noted that the profitability of private banks (return on capital of 30–35%) far exceeds that of most state banks, some of which are loss-making, and argued that state assignments should not restrict the commercial activities of banks [10]. The IMF and the World Bank, in their assessments of the

Uzbek financial sector, emphasize that the dominance of state banks and directed lending remain the main structural weaknesses of the system [7; 11].

The literature review demonstrates a broad consensus that reducing state ownership and lowering barriers to entry increase the efficiency of the banking system. However, the specific dynamics of the Uzbek reform in 2025–2026, including the revised privatization schedule and the rapid growth of digital banks, have not yet been analyzed comprehensively.

METHODOLOGY

The study uses the following methods:

– theoretical analysis of the literature on state ownership of banks and banking competition;

– dynamic analysis of the share of state banks in banking assets for 2019–2025;

– fiscal analysis of the costs of recapitalizing state banks;

– documentary analysis of the privatization strategy and the revised timeline for 2026–2030;

– comparative analysis of the performance of state and private banks;

– SWOT analysis of the banking sector reform.

The data are drawn from reports of the International Monetary Fund, the World Bank, the Central Bank of Uzbekistan, the Ministry of Economy and Finance, and national news agencies.

RESULTS AND DISCUSSION

Dynamics of the state's share in the banking sector. Over the past six years, the share of state banks has declined significantly. According to the IMF, the share of banks with state participation in financial sector assets fell from 84% in 2019 to 67% in 2025 [8]. At the end of 2024, nine state-owned commercial banks held about 65.5% of banking assets and about half of deposits [7]. As of 1 December 2025, the share of state banks in banking assets was 64.53%, or 576.2 trillion soums [9]. The main stages of this process are summarized in Table 1.

Table 1.

Share of state-owned banks in the banking system of Uzbekistan

Period	Indicator	Value
2019	Share of banks with state participation in financial sector assets	84%
End of 2024	Share of 9 state banks in banking assets	65.5%
2025	Share of banks with state participation in financial sector assets	67%
1 December 2025	Share of state banks in banking assets	64.53% (576.2 trillion soums)
2030 (target)	Share of state banks in banking assets	55%

The decline in the state's share was achieved through two channels: the privatization of several banks and the faster growth of private banks. According to the IMF, three state banks were privatized in 2023–2024, and four more were in the process of privatization [7]. The most significant transaction was the sale of Ipoteka Bank to Hungary's OTP Group for USD 324 million [12].

Fiscal costs of state ownership. State ownership of banks has a significant fiscal dimension. Between 2017 and 2023, recapitalizations of state banks from public funds amounted to 0.4–2.0% of GDP annually and about USD 5.8 billion cumulatively, while "policy lending" in the fiscal accounts was 0.9% of GDP in 2023 and 2024 [7]. These figures show that the state has repeatedly had to support its banks, which is consistent with the theory of the soft budget constraint [3]. At the same time, the reported non-performing loan ratio of state banks (3.9% in 2024) was close to the system average [7], but the share of substandard loans was much higher, indicating hidden credit risks.

Privatization strategy and timeline. The updated strategy provides for a gradual reduction of the number of state banks: from nine at present to eight in 2026 and to four by 2030 [9]. The privatization schedule is shown in Table 2.

Table 2.

Planned privatization of state banks (as of January 2026)

Bank	Planned timeline	Notes
Uzsanoatqurilishbank (SQB)	2025–2026 (final stage)	30% stake transferred to the National Investment Fund
Asakabank	2026–2027	EBRD to acquire 15% in 2026
Aloqabank	2026–2027	—
Turonbank	2026–2027	—
National Bank of Uzbekistan, Agrobank, Mikrokreditbank, People's Bank, Business Development Bank	No sale planned for 2026–2028	Remain under state ownership

The privatization of state banks has been delayed compared with the initial plans. Experts cite several reasons: the reduced interest of large foreign banks in acquiring assets in new markets, increased caution of investors because of geopolitical risks in the region, and the small number of potential buyers [10]. An analyst quoted by Kun.uz does not expect the sale of SQB or Asakabank before 2028 [9]. Another factor is that state banks continue to perform state assignments, which reduces their attractiveness for private investors [10].

Competition and the role of digital banks. While privatization has been slow, competition in the banking sector has intensified thanks to the entry and rapid growth of private and digital banks. The Central Bank reports 36 banks operating in the country at the end of 2025 [13]. In 2026, the largest increases in the number of bank cards were recorded by digital banks: Uzum Bank (+2.3 million cards) and Anor Bank (+1.7 million cards), with Uzum Bank becoming the second-largest bank by the number of cards in circulation (7.4 million) [14]. The Uzum ecosystem, which includes Kapitalbank, reported a loan portfolio of USD 3.1 billion and an increase in SME lending of 1.7 times in 2025 [15].

Table 3.

Comparison of state and private banks (selected indicators)

Indicator	State banks	Private banks

Share of banking assets (end-2024)	~65.5%	~34.5%
Share of deposits (end-2024)	about one half	about one half
Return on capital	some negative, only 2–3 above 10%	30–35%
Fiscal support 2017–2023	~USD 5.8 billion recapitalization	—

Table 3 shows that state banks hold a much larger share of assets than of deposits, which means they rely significantly on state and wholesale funding, while private banks are more successful in attracting household deposits. The large gap in profitability confirms the conclusions of the international literature on the lower efficiency of state banks [1]. At the same time, the success of digital banks illustrates the Claessens–Laeven thesis that contestability and the absence of barriers to entry are the key drivers of competition [2].

Table 4.

SWOT analysis of the banking sector reform (author's development)

Strengths	**Weaknesses**
• Clear strategy with quantitative targets • Steady decline of the state's share since 2019 • Successful privatization precedents (Ipoteka Bank) • Rapid growth of digital banks	• Privatization delays • Continued state assignments to banks • High fiscal costs of recapitalization • Hidden credit risks in state banks
Opportunities	**Threats**
• Involvement of international financial institutions (EBRD) • Sale of stakes through the National Investment Fund and IPOs • Digital lending to SMEs • Consolidation of small banks	• Low interest of strategic foreign investors • Geopolitical risks • Concentration of the market in large ecosystems • Risks of rapid consumer credit growth

CONCLUSION

The study shows that Uzbekistan has made significant progress in reducing the role of the state in the banking sector: the share of banks with state participation in financial sector assets fell from 84% in 2019 to about 65–67% in 2025, several state banks have been privatized, and digital banks have become important competitors. However, the state still controls about two-thirds of banking assets, privatization is proceeding more slowly than planned, and the fiscal costs of supporting state banks remain considerable. The updated strategy envisages reducing the number of state banks to four and their share of assets to 55% by 2030.

To strengthen competition and accelerate reforms in the banking sector, the following measures are proposed:

1. Separate state assignments from commercial banking by creating a specialized development institution that would implement state programs, while other state banks operate on a fully commercial basis.

2. Use a variety of privatization methods — sale to strategic investors, IPOs, transfer of stakes to the National Investment Fund and participation of international financial institutions — to overcome the shortage of strategic buyers.

3. Introduce key performance indicators for the management of state banks based on profitability, asset quality and capital adequacy, as recommended by experts.

4. Lower barriers to entry for new banks and fintech companies, including regulatory sandboxes and simplified licensing of digital banks, while maintaining prudential standards.

5. Strengthen the regulation of consumer lending and responsible lending standards to prevent excessive household debt in the context of rapid growth of digital credit.

6. Publish annual reports on the progress of the banking sector strategy, including the share of state banks, fiscal costs and privatization results.

In conclusion, reducing the state's share in the banking sector is a key condition for improving the efficiency of credit allocation and completing the transition to a market economy in Uzbekistan. The combination of privatization, lower barriers to entry and the growth of digital banking can create a competitive financial system capable of financing private sector growth.

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REDUCING THE SHADOW ECONOMY: TAX ADMINISTRATION, CASHLESS PAYMENTS AND INFORMAL EMPLOYMENT

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