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IMPROVING THE MECHANISMS FOR REDUCING STATE OWNERSHIP AND PRIVATISING COMMERCIAL BANKS IN THE TRANSFORMATION OF UZBEKISTAN'S BANKING SYSTEM

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ABSTRACT

Reducing the role of the state in the banking sector is one of the central goals of Uzbekistan's banking reform. The Strategy for Reforming the Banking System for 2020–2025 set the target of raising the share of private banks in total assets to 60 percent. This article evaluates how far this target has been achieved, why privatisation has moved more slowly than planned, and how the mechanisms of reducing state ownership can be improved. The study uses data of the Central Bank of the Republic of Uzbekistan for 2019–2025, a target achievement index, a comparison of state-owned and private banks, a scenario estimate of the efficiency gains from privatisation and an overview of international experience. The results show that the share of state-owned banks in assets fell from 85.0 to 62.4 percent, which corresponds to only about half of the planned shift. Only one large state bank was sold to a strategic investor during the strategy period. State-owned banks continue to lag behind private banks in profitability and asset quality, largely because of their dependence on government funding and directed lending. The article proposes a staged privatisation mechanism that combines balance sheet clean-up, the separation of policy lending, pre-privatisation equity participation of international financial institutions and the use of both strategic sales and public offerings.

Keywords: State-owned banks, privatisation, state ownership, banking reform, strategic investor, IPO, corporate governance, commercial banks, Uzbekistan.

INTRODUCTION

For most of the period since independence, the banking system of Uzbekistan was built around large state-owned banks. These banks served state enterprises, financed government programmes and channelled budget and extra-budgetary funds into priority sectors. This model helped to support investment during the early stages of development, but over time its costs became clear: weak price competition, a high share of preferential loans, limited attention to credit risk and low efficiency of resource allocation.

The Strategy for Reforming the Banking System of the Republic of Uzbekistan for 2020–2025, approved by Presidential Decree No. UP-5992 of 12 May 2020, marked a turning point. The Strategy set the goal of increasing the share of private banks in total banking assets to 60 percent and the share of non-government sources in bank liabilities to 70

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percent by 2025. It also identified a group of large state banks to be transformed and prepared for privatisation with the support of international financial institutions. The sale of a majority stake in Ipoteka-bank to Hungary's OTP Group in 2023 became the first major transaction of this kind.

Despite this progress, the pace of privatisation has been slower than expected. At the end of 2025, banks with state participation still held more than 60 percent of banking assets. The reasons are not only market-related. They also lie in the design of the privatisation mechanism itself: the large volume of government funding on state bank balance sheets, the mix of commercial and policy functions, uneven asset quality and the limited depth of the domestic capital market. Understanding these obstacles is necessary in order to design more effective tools for the next stage of reform.

The aim of this article is to assess the results of reducing state ownership in Uzbekistan's commercial banks and to develop proposals for improving privatisation mechanisms. The study addresses three questions: (1) to what extent have the quantitative targets of the reform been achieved; (2) how do state-owned and private banks differ in efficiency and risk; and (3) which privatisation methods and preparatory measures are most suitable for the remaining state banks.

Literature review

The economic literature generally finds that government ownership of banks is associated with lower efficiency and slower financial development. La Porta, Lopez-de-Silanes and Shleifer (2002), using data for 92 countries, showed that higher government ownership of banks in 1970 was followed by slower financial development and lower productivity growth. Sapienza (2004) found that Italian state-owned banks charged lower interest rates than private banks and that their lending was influenced by the electoral results of the parties affiliated with the bank. Micco, Panizza and Yañez (2007) confirmed that state-owned banks in developing countries tend to be less profitable, with the gap widening in election years.

The effects of privatisation have been examined in a number of comparative studies. Megginson (2005) concluded in his survey that bank privatisation usually improves performance, but the size of the gains depends on the method of sale and the quality of the institutional environment. Clarke, Cull and Shirley (2005) summarised the lessons of privatisation in developing countries and stressed three points: full rather than partial privatisation brings larger gains, sales to strategic investors are more effective than voucher-type schemes, and banks should not be cleaned up repeatedly at the expense of the state, as this creates moral hazard. Boubakri et al. (2005) found that privatised banks in developing countries improved efficiency mainly when control passed to foreign or industrial owners.

Evidence from transition economies is especially relevant for Uzbekistan. Bonin, Hasan and Wachtel (2005) showed that in eleven transition countries foreign-owned banks were the most efficient, while privatisation through the sale of a strategic stake to a foreign investor produced better results than domestic or mass privatisation. Berger et

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al. (2005) demonstrated for Argentina that state-owned banks had poor long-term performance and that privatised banks improved substantially after the change of ownership. At the same time, Cull, Martinez Peria and Verrier (2017) pointed out that state banks may play a countercyclical role during crises, which explains why many governments prefer to keep a minority stake or a dedicated development institution.

Research on Uzbekistan has so far focused mainly on the general direction of the reform. Less attention has been paid to the design of the privatisation mechanism itself, which is the main focus of this study.

Research methodology

The study uses annual data of the Central Bank of the Republic of Uzbekistan (CBU) for 2019–2025, the provisions of the reform strategy and publicly available information on privatisation transactions. Methods of time-series analysis, comparative analysis, target-gap analysis and scenario analysis were applied.

The degree to which the reform targets were achieved was assessed with a target achievement index:

$$TAI = (X_{2025} - X_{2019}) / (X^* - X_{2019}) \times 100\%$$

where X_{2019} is the value of the indicator before the reform, X_{2025} is the actual value at the end of the strategy period, and X^* is the target value. A TAI of 100 percent means full achievement of the planned change.

The potential efficiency gain from privatisation was estimated as the additional profit that state-owned banks would earn if their return on assets partly converged to the level of private banks:

$$\Delta P = A(st) \times [ROA(pr) - ROA(st)] \times k$$

where A(st) is total assets of state-owned banks, ROA(pr) and ROA(st) are the returns on assets of private and state-owned banks, and k is the convergence coefficient ($0 < k \leq 1$) that reflects the share of the gap closed after privatisation.

ANALYSIS AND RESULTS

Achievement of the reform targets. Table 1 compares the main quantitative targets of the Strategy with the actual results at the end of 2025.

Table 1 Achievement of the main targets of the banking reform strategy

Indicator	2019 (base)	Target 2025	Actual 2025	TAI, %
Share of private banks in total assets, %	15.0	60.0	37.6	50.2
Share of non-government sources in bank liabilities, %	48.0	70.0	64.5	75.0
Large state banks sold to strategic investors, units	0	6	1	16.7

Source: author's calculations based on Decree No. UP-5992 and CBU data. TAI – target achievement index.

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The results are mixed. The transformation of the funding base has been relatively successful: three quarters of the planned increase in non-government liabilities has been achieved. In contrast, progress in ownership change has been much more modest. The private share of assets increased by 22.6 percentage points, which is only about half of the planned 45 points, and only one of the large state banks has been sold to a strategic investor.

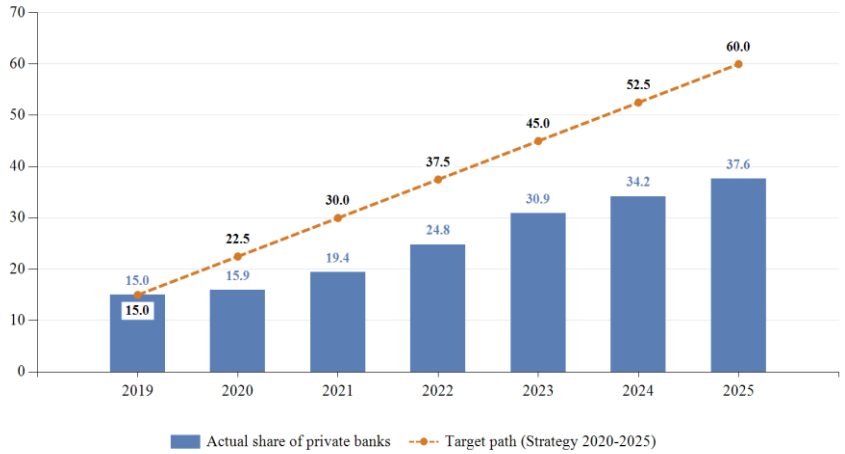


Figure 1. Actual and target share of private banks in banking assets, %
Source: compiled by the author based on Decree No. UP-5992 and CBU data. The target path assumes an even annual increase.

Figure 1 shows that the gap between the target path and the actual share started to widen from 2021. During the first two years the delay could be explained by the COVID-19 shock, but later it reflected structural problems in the preparation of state banks for sale. The acceleration in 2022–2023 was mainly due to faster growth of private banks and the sale of Ipoteka-bank, rather than a systematic reduction of the state's stake across the sector.

Structure of state participation. Table 2 presents the dynamics of the role of state-owned banks in the main segments of the banking market.

Table 2 Role of banks with state participation in the banking system of Uzbekistan

Indicator	2019	2020	2021	2022	2023	2024	2025
Number of banks with state participation	13	13	13	12	11	10	9
Share in total assets, %	85.0	84.1	80.6	75.2	69.1	65.8	62.4
Share in total loans, %	86.4	85.9	83.2	77.1	71.0	67.5	64.2
Share in total deposits, %	69.5	66.8	63.1	57.4	51.9	47.6	45.0
Share of government resources in liabilities of state banks, %	46.8	44.1	39.5	34.2	30.6	27.3	24.9

Source: author's compilation based on CBU data.

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The data reveal an important asymmetry. State banks have lost ground fastest in the deposit market, where their share fell by 24.5 percentage points, while their share in loans declined by 22.2 points. In other words, households and businesses have been moving their savings to private banks faster than lending has shifted. As a result, state banks continue to rely heavily on government resources, which still account for about a quarter of their liabilities (Figure 2).

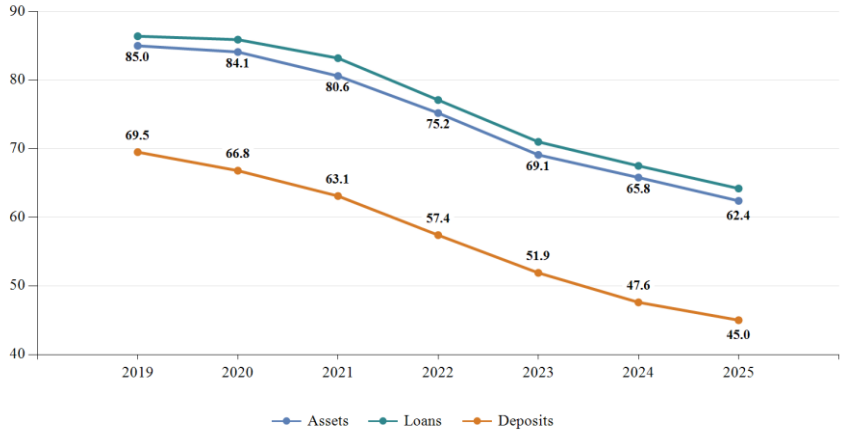


Figure 2. Share of state-owned banks in assets, loans and deposits, %
Source: compiled by the author based on CBU data.

This dependence is one of the main obstacles to privatisation. A potential investor buying a state bank inherits not only its branch network and clients, but also long-term government credit lines tied to specific programmes. These resources are cheap, but they limit the bank's freedom to set prices and select borrowers. Unless the government's funding and policy lending are separated from the commercial balance sheet before the sale, the price offered by investors will remain low and the transaction will be hard to complete.

Efficiency of state-owned and private banks. Table 3 compares the two groups of banks in 2025.

Table 3 Comparison of state-owned and private banks, 2025

Indicator	State-owned banks	Private banks	Banking system
Return on assets (ROA), %	1.4	3.0	2.0
Return on equity (ROE), %	8.9	19.8	12.7
Non-performing loans ratio, %	4.6	2.7	3.9
Cost-to-income ratio, %	40.5	55.6	46.2
Loans to SOEs and under state programmes, % of loans	38.5	9.2	28.0
Loan portfolio growth, %	12.1	31.4	19.3

Source: author's calculations based on CBU data on bank groups.

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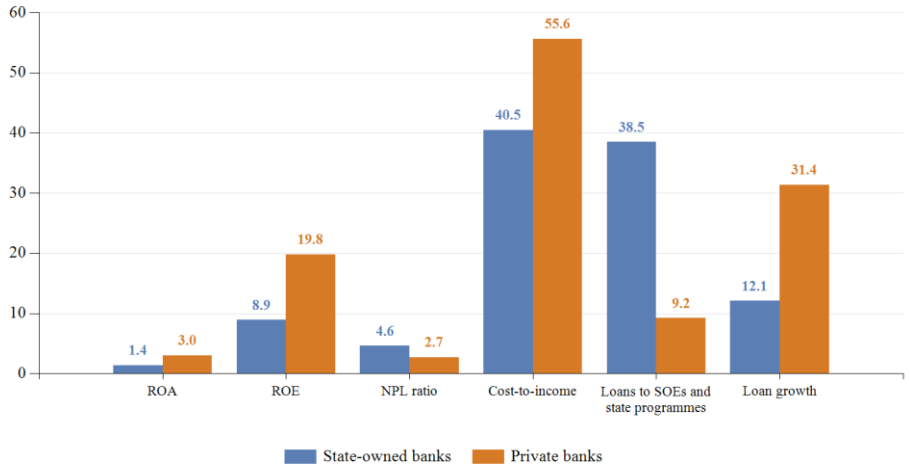


Figure 3. Key performance indicators of state-owned and private banks, 2025, %

Source: compiled by the author based on CBU data.

Private banks earn about twice as much per unit of assets and have a noticeably lower share of problem loans. The only indicator in which state banks look better is the cost-to-income ratio, but this advantage comes from cheap government funding and a concentration on large corporate clients rather than from operational efficiency. Almost 40 percent of the loan portfolio of state banks is directed to state-owned enterprises and government programmes, which explains both their lower returns and their higher credit risk (Figure 3).

Potential gains from privatisation. Using the formula above, the potential additional profit of state banks was estimated under three scenarios. With state bank assets of about 525 trillion UZS at the end of 2025 and a ROA gap of 1.6 percentage points, the full gap corresponds to about 8.4 trillion UZS of annual profit. If privatisation closes one quarter of the gap (k = 0.25), the additional profit would be about 2.1 trillion UZS; with k = 0.50 it would reach 4.2 trillion UZS, and with k = 0.75 about 6.3 trillion UZS. Even the most cautious scenario is comparable to almost one third of the sector's profit in 2024. These figures are approximate, but they show that the cost of slow privatisation is not only institutional but also financial.

International experience. Table 4 summarises several cases of bank privatisation in transition and emerging economies that are relevant for Uzbekistan.

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Table 4 Selected international cases of state bank privatisation

Country	Bank, year	Mechanism	Main result
Poland	PKO BP, 2004	IPO on the Warsaw Stock Exchange, state kept a significant stake	Became the market leader, with better transparency and governance after listing
Romania	BCR, 2006	Sale of a majority stake to a strategic foreign investor (Erste Group)	Fast modernisation of technology and risk management
Kazakhstan	Halyk Bank, late 1990s–2001	Gradual sale of the state stake and stock exchange listing	Largest bank in the country, fully private
Vietnam	Vietcombank, 2007–2011	Partial equitisation via IPO, then sale of a 15% stake to a strategic partner (Mizuho)	State control kept, governance and capital strengthened
Uzbekistan	Ipoteka-bank, 2023	Sale of a majority stake to a strategic investor (OTP Group)	First large privatisation under the 2020–2025 Strategy

Source: compiled by the author based on Megginson (2005), Bonin et al. (2005) and public information on the transactions.

International experience shows that there is no single best method. Sale to a strategic investor brings know-how and quick changes in management, as the Romanian case shows. Public offerings, as in Poland, build a broad investor base and improve transparency, but they require a developed stock market. The Vietnamese model of gradual equitisation allows the state to keep control during the transition, though it limits efficiency gains. What successful cases have in common is careful preparation: clean balance sheets, clear separation of policy functions and credible corporate governance before the sale.

DISCUSSION

The results confirm the conclusions of Clarke, Cull and Shirley (2005) and Bonin, Hasan and Wachtel (2005): the effect of privatisation depends less on the decision to sell and more on how the sale is prepared and to whom. In Uzbekistan, the main constraints are concentrated at the preparation stage. State banks hold large volumes of government funding and directed loans, their asset quality is uneven, and their governance has historically been oriented towards fulfilling state tasks rather than maximising value.

A second issue is the depth of the domestic capital market. The Tashkent Stock Exchange has limited liquidity and few institutional investors, so a large IPO of a state bank is difficult to implement in the short term. For this reason, a combination of instruments seems more realistic: pre-privatisation equity investments by international financial institutions, followed by sale to a strategic investor, and later a public offering

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of the remaining shares. Such a sequence would allow the state to receive a higher price at each step as governance improves.

Third, the reduction of state ownership should not leave gaps in financing priority sectors. Policy lending can be transferred to specialised development institutions with transparent mandates and budget support. This approach also helps to avoid the situation described by Sapienza (2004) and Micco et al. (2007), where commercial banks are used for political or quasi-fiscal purposes. Finally, the state should avoid repeated recapitalisation of banks before sale without changes in management, since this creates moral hazard and weakens market discipline.

Based on the analysis, an improved mechanism for reducing state ownership in commercial banks is proposed (Table 5).

Table 5 Proposed staged mechanism for reducing state ownership in commercial banks

Stage	Main measures	Expected result / indicator
1. Preparation	Independent asset quality review, transfer of problem assets to an asset management company, transfer of state programme loans and related funds to development institutions	Clean balance sheet, share of government resources in liabilities below 10%
2. Governance	Independent board members, competitive selection of management, IFRS reporting and international audit	Governance standards comparable to private banks
3. Pre-privatisation investment	Minority equity stakes of IFIs (EBRD, IFC, ADB) with a clear exit plan	Higher valuation and investor confidence
4. Sale	Choice of method by bank profile: strategic sale for large universal banks, IPO/SPO for banks with a broad retail base	Transfer of control to private owners, growth of private share in assets
5. Post-privatisation	Monitoring of new owners' commitments, full exit of the state from remaining minority stakes through the stock market	Development of the capital market and transparent ownership structure

Source: developed by the author.

The study has limitations. It is based on aggregate and group-level data, and the estimate of potential gains assumes that the performance gap is mainly caused by ownership, while part of it may reflect differences in client base and business model. Bank-level data and event studies of individual privatisation transactions would allow a more precise assessment.

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CONCLUSION AND RECOMMENDATIONS

The study shows that Uzbekistan has made real progress in reducing the role of the state in the banking sector: the share of state banks in assets fell from 85.0 to 62.4 percent, and the funding base became more market-oriented. However, the main target of the reform strategy was achieved only by about half, and the transfer of large state banks to private owners has been slow. State banks remain less profitable and riskier than private ones, mainly because of their policy functions and reliance on government resources. Based on these results, the following recommendations are proposed.

First, a new medium-term programme for reducing state ownership should be adopted with bank-by-bank timelines, clear methods of sale and public reporting on progress. This would increase the credibility of the reform for investors.

Second, before privatisation, the government funding and state programme loans of each bank should be separated from its commercial business and transferred to development institutions. This is the key condition for attracting strategic investors at a fair price.

Third, problem assets should be transferred to a specialised asset management company on market terms, so that buyers acquire a clean bank and the state does not have to recapitalise the same bank more than once.

Fourth, corporate governance of state banks should be brought to market standards in advance, including independent boards, competitive selection of managers and full IFRS disclosure.

Fifth, the method of privatisation should be chosen according to the profile of each bank. Strategic sales are preferable for large universal banks, while IPOs and secondary offerings should be used for banks with a broad retail base and for the final exit of the state, which would also support the development of the domestic capital market.

Overall, reducing state ownership is not an end in itself. Its purpose is to build a banking system in which credit is allocated on commercial principles and banks compete on the basis of efficiency. A well-prepared and gradual privatisation mechanism is the most reliable way to achieve this goal.

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