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EXPANDING THE USE OF ISLAMIC BANKING SERVICES IN FINANCING INVESTMENT PROJECTS IN UZBEKISTAN

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Using effective methods in financing investment projects are vital for minimization of project risks of investment activities in Uzbekistan.

In this case, improving the use of the financial services of rapidly growing Islamic financial institution in the terms of improving the quality of financial services, increasing the capacity of the private sector, improving the living standards of the population, and contributing to the development of the country's economy has been gaining importance in recent years.

At the opening ceremony of the 46th Annual Meeting of the Board of Governors of the Islamic Development Bank (IsDB) took place on

September 3-4, 2021, in Tashkent, Sh.M.Mirziyoyev who is the President of the Republic of Uzbekistan said that “The Islamic world has huge investment potential and energy resources. Moreover, he emphasized that proper use of Islamic financial services will promote expansion of international trade, economic, financial, and investment cooperation with the Member States of Organization of Islamic Cooperation (OIC) member states, and establishing new transport corridors which are connected to our countries will allow achieving high rates of economic development in Uzbekistan[1].

In addition, "We are grateful to the Islamic Development Bank for its timely support of our anti-crisis measures. To this day, the Bank has approved 30 major investment projects in Uzbekistan in health, education, agriculture, water supply, drinking water supply, road infrastructure and construction of affordable housing in rural areas worth over US\$ 2.5 billion” he said.

Furthermore, the address of the President of the Republic of Uzbekistan on December 28, 2020, "It is time to create a legal framework for Islamic finance," which shows once more the importance of this sector and its role in economic development in our country [2].

Therefore, it is necessary to attract funds from investment funds, organisations and existing banks were based on Islamic finance in Muslim countries in order to support the socio-economic development of Uzbekistan and expanding opportunities for financing investment projects.

Nowadays, Islamic financial institution is one of the fastest-growing and most reliable sectors in the world, with a total of \$ 2.88 trillion in assets, which is growing by 15-20% annually.

In 2004, Uzbekistan became a member of the Islamic Corporation for the Development of the Private Sector. The IDB Representative in Uzbekistan began its work in October 2006 in Tashkent.

Since that time there have been offered some Islamic financial services in financing a number of investment projects which have been analyzed below.

Currently, Uzbekistan has been considering the issue of joining two other organizations of ITB which are the Islamic Corporation for Investment and Export Credit Insurance (ICIEC) and the International Islamic Trade and Finance Corporation (ITFC).

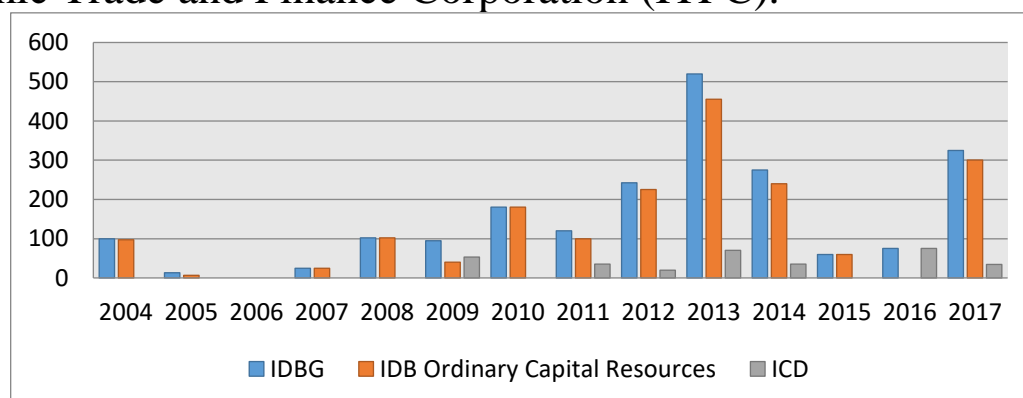


Figure 1. Funds provided by ITBG for Uzbekistan (*USD in millions*)[3].

From the given figure 1, it can be seen that the amount of projects have been approved by the Islamic Development Bank for Uzbekistan which is 2.1 billion USD, of which 304 mln. USD belongs to ICD and 1.82 bln. USD the share of the ITB in the given period.

In 2010, an initial leasing company named “Toiba Leasing” was founded by ICD with a charter capital of \$ 5 million, also provided its Sharia-compliant leasing services to the private sector. In the shown period (2010-2017), the company financed more than 200 worth of projects included USD 26.3 mln.

Tables 1 and 2 summarize the IDB's financing methods for Uzbekistan and its sectoral financing portfolio.

In terms of financing methods, the first place was occupied by istisna (model for construction works), the second and third places were taken by murabaha (sale in installments) and ijara (leasing).

Table 1. IDBG portfolio for Uzbekistan in terms of financing methods [3].

Methods of financing	Projects		
	number	mln. I.D.	mln. USD.
Technical support	5	0,8	1,1
Credit	3	22,2	32,5
Special assistance operations	8	1,4	1,9
Sell to pay in installments	11	292,4	446,0
Istisna	12	616,7	909,3

Co-financing lines	3	29,4	45,0
Capital	1	3,2	5,0
Leasing	11	275,7	412,1
Trade finance	19	199,6	292,6
Total	73	1,441,4	2,145,5

The results, as shown in Table 1, indicate that the main share of projects (45.4%) were the construction and building materials industry while, the second, third, and fourth places were gained by light industry (14.87%), transport services (4.96%) and food production (4.95%) respectively. The share of other sectors was 29.8 % in total and less than 4 % on an individual basis.

It can be seen that construction-oriented projects were the main part of the financing, which included the reconstruction of irrigation systems, road construction, construction of schools, colleges, and other projects.

Funding by ICD was mainly used as Murabaha contracts, and more than 70% of it directs on lines of financing through banks, and the remaining 30% was direct financing. These projects of the ICD contribute to the development of various sectors of the economy, in particularly, including pharmaceuticals, healthcare, construction materials, textiles, food industry, agriculture, and others.

Table 2. Financing portfolio of IDB and ICD for Uzbekistan shown in the part of the sectors

Sector	Projects								
	IDBG (Total)			In particular					
				IDB			ICD		
	Numb er	mln. I.D.	mln. USD.	Numb er	mln. I.D.	mln. USD.	Numb er	mln. I.D.	mln. US D.
Education	12	52,3	78,6	5	51,1	77,0	0	0,0	0,0
Finance	17	189,3	279,7	4	29,6	45,1	10	151,8	223,0
Health care	9	81,0	118,5	3	53,0	78,3	5	27,8	40,0
Industry and mining	9	41,1	61,1	2	13,7	20,0	7	27,4	41,1
Information and communication	0	0,0	0,0	0	0,0	0,0	0	0,0	0,0

technologies									
Transport	4	228,6	348,0	4	228,6	348,0	0	0,0	0,0
Energy	8	350,0	533,1	8	350,0	533,1	0	0,0	0,0
Agriculture	8	436,8	632,6	8	436,8	632,6	0	0,0	0,0
Real estate	0	0,0	0,0	0	0,0	0,0	0	0,0	0,0
Water supply, sanitation and municipal services	2	61,7	92,9	2	61,7	92,9	0	0,0	0,0
Others	4	0,7	1,0	4	0,7	1,0	0	0,0	0,0
Total	73	1,441,4	2,145,5	40	1,225,2	1,828,0	22	207,0	304,1

As follows from the table shown above, the projects have been approved for financing by the Islamic Development Bank Group by sector, the largest investment was directed to the agricultural and rural development sector, which accounted for almost 30% of the ITBG portfolio. After the figure, it was followed by energy with a share of 25%, transport (16%) and finance (13%) respectively.

Despite being the last of the CIS countries to join the IDB and ICD, Uzbekistan ranks first in the portfolio of both organizations in the region.

In March 2018, it was signed between the Government of Uzbekistan and the ITFC about 100 million USD allocated to finance trade operations. According to this contract, the corporation has got a chance to finance trade projects before being a member of Uzbekistan in the organization, and to date, the ITFC has provided a line of financing based on Murabaha to the Asian Alliance Bank, Trustbank, and Kapital Bank.

In addition, by 2021, the Islamic Corporation for the Development of the Private Sector (ICD) has signed agreements to open windows providing Islamic financial products and services ("Islamic windows") in several commercial banks in Uzbekistan. The launch of these windows is scheduled for the second half of 2021 [4].

The Islamic window is in most cases set up in countries where there is no Islamic financial system or legislation on Islamic finance.

Because, the Islamic window offers a limited number of services and products as a product of a traditional bank, based on the existing laws and legal framework of a particular country.

Islamic banking services and products are usually completely provided after the relevant laws have been enacted in that country. Therefore, the most common purpose of establishing Islamic windows is to:

- 1) To study the demand for Islamic financial services in the country;
- 2) Offering Islamic financial services on the basis of the existing infrastructure (buildings, staff, etc.) in conventional banks without additional costs;
- 3) To make practical proposals for the development of a law on Islamic finance and banking in the country through the study and in-depth analysis of the activities of established Islamic windows;
- 4) Increasing their participation in the country's economy by increasing the financial literacy of the population and the private sector;
- 5) Development of future development strategies of banks based on the analysis of the results of the Islamic window.

In conclusion, from the outcome of our investigation, it is possible to conclude that Islamic finance is a new field for the Uzbek economy but it is necessary for both entrepreneurs and individuals. Moreover, the emergence of alternative financing products will promote to expand of financial assets in order to finance investment projects in the country. However, existing expectations can be seriously distorted due to the lack of experience and knowledge of potential customers in the field of Islamic finance, as well as insufficient improvement of banking and financial legislation in Uzbekistan.

Furthemore, our research demonstrated that current legislation prohibits commercial banks to offer Islamic finance services. In particular, current tax and banking legislation does not allow conventional banks to buy and sell Islamic products.

As it is not generally agreed that tax law in Uzbekistan, if banks finance equipment or technology under Islamic finance, they have to pay value-added tax (VAT) or cannot be allowed to charge a payment for late in Islamic finance, and even if they are taken for disciplinary

purposes, the money is credited to a separate account and used for charity. However, this fine is considered as a profit by the tax authorities and charged as a tax.

Therefore, the Islamic window in this case can be solution for the issue before offering whole Islamic financial services in order to study the demand for Islamic financial services in the country.

On the basis of the promising findings presented in this paper, work on the remaining issues is continuing and will be presented in future papers.

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ХИТОЙНИНГ МАРКАЗИЙ ОСИЁГА ТАЪСИРИ

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Тахминан ўттиз йил мобайнида Хитой ва Марказий Осиё ўртасидаги муносабатлар жуда динамик эди. 90 йилларнинг бошидан Хитой дунёнинг етакчи давлатларидан бирига айлана бошлади.

Хитойнинг Марказий Осиёдаги сиёсати Пекин учун жуда муҳим. Аммо у олий раҳбарият учун катта аҳамиятли эмас. 90-йиллар бошида Марказий Осиё давлатлари эндигина мустақилликни қўлга киритганда, бу ташқи сиёсатнинг муҳим йўналишларидан бири саналган. Айниқса, Пекин учун чегарадош давлатларда тинчлик бўлиши муҳим эди. Айни пайтда Марказий Осиё давлатлари барқарор ривожланишга, хавфсизлик етарлича