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SUBSTANTIAL INVESTMENTS IN THE POWER SECTOR ARE EXPECTED THROUGH THE PUBLIC PRIVATE PARTNERSHIP (PPP) MECHANISM. FOR EXAMPLE, WITH THE SUPPORT OF THE INTERNATIONAL FINANCE CORPORATION (IFC), A PILOT PROJECT (AS PART OF SCALING SOlar PROGRAMME) IS BEING IMPLEMENTED TO BUILD A 100MW SOLAR PHOTOVOLTAIC (PV) STATION IN THE NAVOIY REGION. THE INTERNATIONAL COMPETITIVE TENDER RECENTLY ENDED WITH FIVE BIDDERS, NAMELY ‘TOTAL EREN’ (FRANCE), TBKA SOLAR (CHINA), MASADDR (UAE), ACRUA POWER (SAUDI ARABIA) AND JINKO SOLAR (CHINA), REACHING THE FINAL STAGE. MASADDR WON THE TENDER WITH THE OFFER OF 2.679 US CENTS PER KWH. GIVEN THE SUCCESS OF THIS TENDER, WE ARE SOON TO LAUNCH TWO MORE TENDERS FOR 900MW SOLAR PV STATIONS.

MOREOVER, TRANSACTION ADVISORY MANDATES HAVE BEEN SIGNED FOR A FURTHER 1,300MW CGGT GREENFIELD PROJECT IN THE SIRDARYA REGION WITH THE IFC AND FOR A 1,000MW SOLAR PV PROJECT IN THE SURKHANDARYA REGION WITH THE ADB. THESE PROJECTS WILL PAVE THE WAY FOR MORE PPP-BASED CONVENTIONAL AND RENEWABLE ENERGY PROJECTS. BY 2030, WE PLAN TO INCREASE THE INSTALLED CAPACITY OF SOLAR POWER PLANTS TO 5,000MW. FURTHERMORE, THROUGH THE PPP MECHANISM, WIND (2,000MW) AND GAS-FIRED CGGT (3,400MW) POWER STATIONS ARE ALSO PLANNED BY 2030.

IN THE OIL AND GAS SECTOR, THE INVESTMENT PROGRAMME FOR THE NEXT DECADE IS ESTIMATED AT $34BN, CONSISTING OF 40 PROJECTS INCLUDING EXPLORATION, DEVELOPMENT, TRANSPORTATION AND STORAGE OF NATURAL GAS AND PETROCHEMICAL PROCESSING. A SUBSTANTIAL PROPORTION OF THESE INVESTMENTS WILL BE COVERED THROUGH FDI. THEREFORE, THE GOVERNMENT IS KEEN TO OPEN UP FURTHER NEW INVESTMENT BLOCKS FOR FOREIGN INVESTORS. THIS, TOGETHER WITH INVESTMENTS IN UZBEKNEftegaz, WOULD INCREASE THE DOMESTIC PRODUCTION OF NATURAL GAS TO 74.8BN CUBIC METRES (+23% VS 2018) AND LIQUID HYDROCARBONS TO 7.1M TONNES (+130% VS 2018) BY 2025.

IN CHEMICALS, TOGETHER WITH BOSTON CONSULTING GROUP, WE HAVE DEVELOPED OUR STRATEGY 2030 BASED ON THREE PRIORITY AREAS: FERTILISERS, GASOCHEMICAL AND OTHER CHEMICAL PRODUCTS. THIS STRATEGY MOSTLY RELIES ON FDI (THROUGH PRIVATISATION AND GREENFIELD INVESTMENTS) WHICH HAS ALREADY STARTED WORKING WITH INDOMARA CORPORATION FIRMLY ON THE GROUND. AT THE MOMENT, SEVERAL SOEs PRODUCING FERTILISERS ARE UP FOR SALE.

CORPORATE GOVERNANCE AND INSTITUTIONAL DEVELOPMENT

THE GOVERNMENT IS KEEN TO IMPROVE CORPORATE GOVERNANCE IN SOEs. TOGETHER WITH INTERNATIONAL ORGANISATIONS SUCH AS THE WORLD BANK, ADB, EBRD AS WELL AS LOCAL AND INTERNATIONAL CONSULTING FIRMS, WE HAVE IDENTIFIED KEY AREAS OF CONCERN. BASED ON THAT, THERE IS A FIRM COMMITMENT AND POLITICAL WILL TO ADDRESS THESE CONCERNS.

AS A RESULT, MORE TRANSPARENCY, INDEPENDENT DIRECTORS, IFRS IMPLEMENTATION, CREDIT RATINGS AND ACCESS TO CAPITAL MARKETS (INCLUDING IPOs) ARE REFLECTED IN ALL THE ROADMAPS TO REFORM THE SOEs. TO ILLUSTRATE, UZBEKNEftegaz AND UZTRANSgAZ WILL HAVE IFRS REPORTING IN 2020 WHILE THERMAL POWER PLANTS, UZHYDRO AND NATIONAL ELECTRIC SYSTEMS WILL MOVE TO IFRS BY 2021. THE WORLD BANK, ADB AND EBRD HAVE CONFIRMED THEIR COMMITMENT TO ASSIST NEWLY FORMED POWER COMPANIES IN CORPORATE GOVERNANCE IMPLEMENTATION, INCLUDING SELECTION OF INDEPENDENT DIRECTORS WITH INTERNATIONAL EXPERIENCE.

IT IS IMPORTANT TO MENTION THAT A FOCUS ON CORPORATE GOVERNANCE IS HAPPENING WITHIN THE FRAMEWORK OF A BROADER STRATEGY TO STRENGTHEN INSTITUTIONS IN UZBEKISTAN. DEVELOPMENT STRATEGY 2017-2021 IS BASED ON FIVE Pillars, Including Development of the Institutional Framework of the State Administration and Rule of Law and Legal Reforms.

TO MEASURE OUR PROGRESS IN STRUCTURAL REFORMS, THE GOVERNMENT IS FOLLOWING 24 GLOBAL RATINGS AND INDICES, INCLUDING WORLDWIDE GOVERNANCE INDICATORS (WORLD BANK) AND THE CORRUPTION PERCEPTION INDEX (TRANSPARENCY INTERNATIONAL). LINE MINISTRIES AND AGENCIES HAVE DEVELOPED ROADMAPS WITH CLEAR MILESTONES TO IMPROVE EACH INDICATOR. WHILE THE PROGRESS MAY TAKE TIME, WE BELIEVE WE ARE ON THE RIGHT PATH WITH THE RIGHT PARTNERS.

VISION

OUR LEADER, HIS EXCELLENCY PRESIDENT SHAVKAT MIRZIYOYEV, HAS SET AMBITIOUS OBJECTIVES FOR THE GOVERNMENT. WHEN WE SUCCEED, UZBEKISTAN WILL BE A DIFFERENT COUNTRY WITH A MODERN ECONOMY AND WELL-FUNCTIONING ENERGY MARKET BENEFITTING FROM STRONG PRIVATE SECTOR PARTICIPATION.
Uzbekistan's energy sector at the threshold of major reforms

By 2025, the share of electricity production using renewable and alternative energy sources is planned to increase to at least 20% of total generation.

Uzbekistan's turbulent past has left its mark on every aspect of the country's economic and social life, but we are now looking to the future. The new government, headed by President Shavkat Mirziyoyev, is searching for ways to reform outdated managerial and technological practices and bring the country into the 21st century.

Several government decrees have been adopted recently aimed at radically increasing the efficiency of fuel and energy complex management as well as switching to modern methods of organising the production, transportation, distribution and marketing of electricity both within Uzbekistan and beyond its borders.

The energy sector rightly deserves special consideration. Uzbekistan is one of the most energy-intensive economies in the world and its industrial sector, which utilises inefficient and obsolete technology in its production processes, accounts for around 40% of total energy consumption. For years this sector was run using non-economic methods, a practice which is no longer sustainable.

In the power generation industry, the most critical problems are the growing shortfall of electricity supply and significant wear and tear on equipment, including the distribution networks. According to analysts, one of the main causes is the insufficiently effective management of the electricity industry and historical underinvestment into new technologies throughout the sector.

To help find solutions to the growing problems within the sector, a new Ministry of Energy was established, tasked by the state to deal with all issues related to the fuel and energy sector of the country. The Ministry of Energy now directly includes the Uzatom Agency, Uzbekneftegazinspection, Uzenergoinspection, and the Implementation Group, which co-ordinates projects under production sharing agreements.

The Ministry also co-ordinates the activities of the Uzbekneftegaz, Uztransgaz and Regionalalgaz joint stock companies, as well as the entities created from Uzbekeenergo JSC: Thermal Power Stations, National Electric Grids of Uzbekistan and Regional Electric Grids.

It is also important to address the expected shortage of natural gas, which is today the main raw material for electricity generation, along with the inadequate energy-saving measures by modern standards and the significant untapped potential for the use of renewable energy sources.

A significant role in ensuring the country's energy efficiency is given to diversification of energy sources. To this end Uzbekistan has made a historic decision to begin the development of nuclear energy generation.

The Agency for the Development of Atomic Energy of Uzbekistan was founded in July 2018, and in October last year, a project was launched to build the country's first nuclear power plant using Russian technology.

In May 2019, two new laws were adopted in Uzbekistan: “On the use of renewable energy sources” and “On public-private partnership”. This created a legislative basis for attracting investment in the energy industry, as well as a system of incentives for users and manufacturers of renewable energy equipment.

By 2025, the share of electricity production using renewable and alternative energy sources is planned to increase to at least 20% of total generation.

The fundamental reform of the fuel and energy complex also applies to the oil and gas industry. For decades, the industry has been driven by non-economic methods, which led to lags in the growth of hydrocarbon reserves and an increasing deficit in natural gas, especially in the private enterprise sector.

In July 2019, a resolution of the President was adopted, aimed at large-scale reform of the industry. During the restructuring, excessive intermediate management links have been reduced through the merger of subholding companies of Uzbekneftegaz and the withdrawal of Uztransgaz from this system.

Uzbekneftegaz's stake in the authorised capital of Uztransgaz has been transferred to the state through the State Assets Management Agency.

EFFICIENCY DRIVE

Measures to improve the efficiency of processing, transportation and sale of natural gas, and analysis and optimisation of investment projects were identified. Uzbekneftegaz has begun the process of improving mechanisms for the sale of finished products, strengthening financial discipline and optimising pricing at enterprises in the oil and gas industry.

The process of reforming the fuel and energy sector is based on accumulated experience, analysis and support of the best international models. World experts in this area have been engaged and substantial assistance is being provided by international financial institutions (IFIs).

For example, the World Bank is supporting projects to increase the energy efficiency of district heating, develop the energy market, and modernise the mechanism of electric power transmission. Energy efficiency will help minimise operating and maintenance costs, improve productivity and generate real cashflows. It will also contribute to mitigation of the effects of climate change.

The Asian Development Bank is promoting regional co-operation projects to expand cross-border energy trade and integrate renewable energy sources into the grid, develop sustainable hydropower projects and increase the efficiency of electricity production.

The European Bank for Reconstruction and Development is participating in the implementation of the Tashkent nuclear energy project and modernisation of the Tashkent central and Muruntau transmitting stations.

Uzbekistan's economy has been developing rapidly in recent years, leading to a significant increase in energy consumption. Over the next 10 years we expect consumption to more than double. It is therefore crucial to ensure the country's energy security, taking into account the constant growth of needs, reforming of managerial styles, attracting foreign investment and creating new jobs.

This complex and demanding work is being done today with the assistance of IFIs and consultants as well as dedicated efforts by the Uzbekistan government, its new Ministry of Energy and thousands of people in the sector who are building for future generations.
By Lucy Fitzgeorge-Parker

Even by the standards of Central Asia, Uzbekistan is rich in natural resources. The country boasts more than 270 hydrocarbon deposits and is second in the region for natural gas production, and in the top 20 globally.

A recent independent audit put Uzbekistan’s reserves of natural gas at more than one trillion cubic metres, while liquid hydrocarbon reserves are estimated at around 150 million tonnes. Income from the oil and gas sector accounts for 10% of GDP and 15% of budgetary revenues.

Unfortunately, the potential of the industry has not previously been fully realised due to inefficient management and lack of investment in exploration, infrastructure and technology.

As a result, despite an 8% increase in natural gas production in Uzbekistan over the past 20 years, the proportion produced by Uzbek firms has fallen to 29%. Moreover, for the past five years, the rate of natural gas reserves replacement has averaged barely 70%.

The sector is clearly ripe for reform — and, under new president Shavkat Mirziyoyev, policymakers have taken up the challenge. In 2018, a comprehensive study of the oil and gas industry was commissioned by the government, with the backing of the Asian Development Bank.

“We were given the goal of working out how to bring the sector up to international standards,” says Ulugbek Ashurov, deputy chairman of Uzbekneftegaz. “We spent a year studying the practices of international oil companies, as well as taking an inventory of the situation in Uzbekistan.”

The results of this investigation were revealed in July, when President Mirziyoyev laid out plans for a radical overhaul of Uzbekistan’s energy industry.

At the heart of the government’s programme is a major restructuring of state-owned oil and gas giant Uzbekneftegaz (UNG).

This included the merger of four subsidiaries of UNG — drilling company Uzborneftegaz, oil and gas producer Uzneftegazdobyche, petroleum refining firm Uznefteprodukt, and machinery and equipment manufacturer Uzneftegazmasch — with the parent company.

Six oil and gas producing and processing entities were also brought under the direct management of UNG, while all the company’s service companies and nearly 300 non-core assets were marked for disposal.

UNG is now responsible for upstream and downstream operations in the state sector, comprising exploration, production, recycling and reproduction.

Midstream operations have been handed to Uztansgaz, which has been unbundled from UNG and transferred to the ownership of the Agency for Management of State Assets.

As well as sole responsibility for Uzbekistan’s high-pressure pipelines, Uztansgaz’s remit includes purchasing natural gas from extraction and processing organisations, and selling it to end users and new regional gas distribution entity Hudugdazaminot.

The latter was established to manage the local distribution of gas to consumers within Uzbekistan, with responsibilities including the operation and maintenance of distribution networks, and the purchase, storage and sale of liquified gas to consumers.

Hudugdazaminot’s corporate structure includes 14 local distributors, which have been earmarked as potential candidates for foreign investment through public private partnerships.

REFORM IMPLEMENTATION

A working committee, chaired by prime minister Abdullo Ariporov, has been established to oversee the implementation of the government’s programme for the energy industry.

The committee has been tasked with monitoring the progress of reforms, ensuring continued technical and financial support from international development institutions, government bodies and consultants, and approving roadmaps for the achievement of the key goals of the project.

These include modernising Uzbekistan’s gas transmission system — more than half of the country’s 13,000km of main gas pipelines are more than 30 years old and 58% of its gas compressor units need replacing — and, above all, increasing hydrocarbon production volumes.

This will be achieved both through exploration and the enhanced exploitation of existing fields in conjunction with leading international oil and gas companies.

On the exploration side, UNG is already working with long-standing global partners including Russia’s Lukoil and Gazprom, China National Petroleum Corporation and Korea National Oil Corporation, as well as new market entrants from countries including the UK, France, India and Azerbaijan.

The Uzbek government has announced plans to offer more than 50 investment blocks to foreign investors, with a focus on hard-to-recover hydrocarbon fields. Indeed, the decree mandates the transfer of the latter to companies with relevant experience.

The expansion of geological exploration of poorly studied areas and blocks with complex geological structure is already under way with the help of foreign firms including Total, BP, Mubadala Petroleum, SOCAR, Thyssen Krupp, Tatneft, ONGC Videsh and Epsion Development.

Tatneft and Mubadala Petroleum, along with other companies from Russia and the United Arab Emirates, are also working with UNG on increasing hydrocarbon production in depleted, stripped and suspended oil and gas fields, as well as those with hard-to-recover reserves.

Ashurov notes that the increase in production will help to meet a rise in demand for hydrocarbons driven by the rapid growth of the Uzbek economy. GDP is expected to expand by at least 5% over the coming years as the government’s reform agenda bears fruit.

The increase in domestic demand may be muted, however, by a parallel programme to improve energy efficiency in Uzbekistan, both in industry and in the household sector.

That will increase the potential for a substantial rise in natural gas exports. Already more than 15% of Uzbekistan’s natural gas production is sold outside the country. Some goes to Russia but most goes east, to Tajikistan, Kyrgyzstan, the south of Kazakhstan and China.

Ashurov sees great opportunities for UNG to serve rising demand from China for natural gas. “China is a huge market and we can see that they are now implementing a policy of moving away from coal towards cleaner energy sources,” he says. “Natural gas is a much safer and more ecological product.”

UNG is also looking to develop new export markets for both natural gas and other hydrocarbon products.

“We know there is huge demand for natural gas in India and Pakistan, and we are ready to enter discussions with those countries,” says Ashurov.

“We also see opportunities for exporting products such as LPG gasoline to Tajikistan and we are exploring the options for working in Afghanistan, which could be a major export market for us.”
PETRO INDUSTRY DEVELOPMENT

Another key objective of the government’s reforms is the development of Uzbekistan’s petrochemical industry, particularly in the sphere of high value-added products. Responsibility for this part of the programme has been assigned to UNG, along with state-owned chemical producers Uzkimmysanoat.

“We are currently solving a large-scale task of extracting valuable components from available raw material resources by means of their deep processing,” says Ashurov.

Progress is already being made in this area. Over the past two years, a number of key projects have been implemented, including the development of a complex of fields at Kandy.

In April 2018, a new gas processing facility with an annual production capacity of 8.1 billion cubic metres of hydrogen sulphide-containing gas was commissioned at the site. The complex is jointly owned by Lukoil and UNG, and was funded by international banks including ING, UniCredit and Deutsche Bank.

Kandy is located in the Bukhara region, which is also home to one of Uzbekistan’s largest refineries. A second major refinery, in the Fergana region, is one of the facilities where policymakers are hoping to bring in foreign investment.

Investment highlights: oil and gas

OIL

The construction of a plant for the production of synthetic liquid fuel (GTL) based on purified methane from the Shurtan Gas Chemical Complex

The plant will produce high-quality diesel and aviation fuels that meet stringent environmental standards, unparalleled in quality and the absence of harmful impurities. The total cost of the project: $2bn, financed by Korea Exim Bank, along with 15 commercial banks.

Creation of a gas-chemical cluster based on methanol-to-olefins (MTO) technology.

This will enable the manufacture of new types of products, such as polyethylene terephthalate, polystyrene, polyvinyl chloride, propylene oxide polyol, gasoline and diesel fuel, in accordance with the requirements of Euro-5. This project is in collaboration with Air Products and Mubadala, as well as engineering and construction companies from South Korea and Singapore.

GAS

A joint venture with Forus JSC, a Russian company, to reconstruct the storage facility at Gazli. This will more than triple the gas storage capacity to 10 billion cubic metres. Work is already underway on the first phase of the project, which will double the storage capacity to six billion cubic metres by the end of 2021. The second phase is due to be completed in 2024. Infrastructure at the facility will be modernised in parallel with the reconstruction work. The total cost of the project: $850m.

A new gas processing facility with intended annual production capacity: 8.1 billion cubic metres of hydrogen sulphide-containing gas

The complex is jointly owned by Lukoil and UNG, and is funded by international banks including ING, UniCredit and Deutsche Bank.

Uzbekistan Independence’ gas field in the southern Surkhandarya region

In 2017 the Government of Uzbekistan signed a production-sharing agreement with Swiss and Cypriot investors and Uzneftegazdobycha. The total cost of the project: $5bn.

The first phase of the project, due to be completed by 2023, will see the construction of a gas processing plant with a capacity of five billion cubic meters of natural gas per year. That will be followed within three years by the construction of a gas chemical complex with a production capacity of 500,000 tonnes of polymer products.
ENERGY COMPANY UNG LOOKS TO GIVE WARM WELCOME TO FOREIGN INVESTORS

GlobalMarkets: How has the government’s strategy for the energy sector affected Uzbekneftegaz (UNG)?
Ulugbek Ashurov: Our primary task is to create a new vertically integrated company that corresponds to international standards of efficiency, transparency and corporate governance. We have already started our work on the transformation of the company. We began by realising nearly 300 non-core assets, a process which is due to finish by the end of this year.

We have also started work on the sale of our service companies, which will take place next year, in order to increase competition in the market and lower the price. This will be done under open tender and we expect the majority of buyers to come from the private sector.

The next step is to make the company more attractive for public market investors. Our financial statements have been audited by EY for the past three years and we are currently preparing to move to IFRS standards at the start of next year.

We are also working on improving our corporate governance. We have created a supervisory board and are planning to appoint independent directors with good experience of the international oil and gas industry. The process is already underway and we expect it to be completed by the end of the year.

In addition, we are looking to appoint executives from outside Uzbekistan to our management board. We are currently recruiting internationally for a first deputy chairman, who will be responsible for the implementation of our investment programme, and for our deep processing and downstream projects.

Once we have completed our organisational restructuring, we want to achieve an international credit rating and then issue a Eurobond.

GM: What is capital markets access important for UNG?
UA: We want to change the way we fund ourselves. Until now, all our financing has come directly from the state or with a sovereign guarantee. We want to issue a Eurobond in order to diversify our funding sources and reduce our reliance on government support.

We have had discussions with large investment banks and financial institutions, and the feedback we have received is that there is strong appetite for our bonds among global investors.

Some banks have encouraged us to come to market this year, but we believe it is important to finish our corporate transformation first. What we are hearing from investors is that their top priority is having access to high-quality and transparent financial statements.

Once we are confident that we are up to international standards, and have seen an increase in our production levels, then we will be ready to issue a Eurobond.

After that, the government’s strategy calls for the privatisation of UNG via an IPO before the end of 2024. We will remain state-controlled but investors will have an opportunity to buy up to 49% of the company.

Before that, however, we will need to make substantial improvements to our profitability and our production capacity.

GM: What level of investment does UNG require?
UA: We have around 40 projects lined up for the next 10 years with a total cost of around $34bn. We expect half of this to come from foreign direct investment and loans.

GM: Where do you see the greatest opportunities for development?
UA: The investment policy of UNG is aimed firstly at replenishing reserves and increasing hydrocarbon production with the use of advanced technologies, carrying out geological exploration on poorly explored and complex subsoil areas, and intensifying production at fields with hard-to-recover reserves.

We want to modernise and improve the efficiency of our existing oil refineries, as well as introducing advanced information and communication technologies across the industry. We want to digitalise all our processes, starting with our wells and finishing with the distribution of our final products.

It is also important to remember that the energy sector in Uzbekistan not only covers the extraction of resources from the earth but also the system of complexes for processing raw materials and manufacturing products.

We want to deepen the processing of hydrocarbons and introduce new high added-value petrochemical products to serve the domestic market and for export.

GM: What are the key development projects in this area?
UA: One of our biggest projects is the construction of a plant for the production of synthetic liquid fuel (GTL) based on purified methane from the Shurtan Gas Chemical Complex, which is one of the world’s largest gas processing and polymer production plants.

The plant will produce high-quality diesel and aviation fuels that meet stringent environmental standards, unparalleled in quality and the absence of harmful impurities. The project will cost $3.7bn and is being financed by our own resources at UNG and international loans.

We are also implementing a series of large projects, one of which is modernising of the Bukhara refinery, that allows the release of high-quality fuel — gasoline and diesel fuel — in accordance with the requirements of the Euro-5 Directive.

Furthermore, work is underway to establish a gas chemical cluster based on methanol-to-olefins (MTO) technology. We are collaborating on this project with Air Products, as well as with the engineering and construction companies from South Korea and Singapore.

The implementation of the gas chemical cluster project will allow the production of new types of products, such as polyethylene terephthalate, polystyrene, polyvinyl chloride, propylene oxide poloyl.
UZTRANSGAZ TRANSFORMATION AIMS TO FUEL UZBEKISTAN’S ECONOMIC GROWTH

Our key focus areas are the modernisation of our gas transportation system, and the expansion of export and transit opportunities

GlobalMarkets: What is your goal for the next five years?
Sayidov Ulugbek: Our mission is to transform Uztransgaz into a world-class company in collaboration with international experts.

The first tasks are to make the company profitable and self-sustaining, and to achieve the highest standards of corporate governance. We want to make sure every aspect of our operations is fully transparent, from human resources and procurement to the realisation of investment projects.

To achieve this, we are bringing in external consultants in all areas with the support of a grant from the Asian Development Bank (ADB).

We are currently working to move to IFRS reporting standards from the start of next year and to obtain an international credit rating. We will then raise funding through the Eurobond market. We will also continue to attract long-term financing from international financial institutions.

After that, we will start to prepare to undertake an IPO before the end of 2024, as mandated by the president’s decree of July 9.

The size of the initial stake to be sold has yet to be determined. However, the state will retain at least 51% of the company. This is because we have a natural monopoly and it is important for the government to be able to guarantee all production companies access to the gas transportation system.

There is a lot of work to be done but we understand the challenges. I am confident that in three years Uztransgaz will be a very different company, based on the direction of travel set by our president.

GM: When do you expect Uztransgaz to be profitable?
SU: If prices were based solely on market mechanisms we would be profitable. However, at the moment, some sectors are still receiving gas at below-market prices.

The government is working hard to close this gap. Tariffs were increased on August 15 and, as a result, we expect to show a full-year profit in 2020.

The purpose of unbundling Uztransgaz from Uzneftegaz was to make the company profitable and reduce its dependence on government support.

GM: How much investment does Uztransgaz need?
SU: Our key focus areas at present are the modernisation of our gas transportation system, and the expansion of export and transit opportunities.

More than half of our main gas pipelines are more than 30 years old. We also urgently need to upgrade our network of gas compressor units. We have 250 units in total, of which 145 are outdated and need renovating or replacing.

We want to work with a single international partner on the gas compressor network project and will put it out to public tender.

We estimate the total cost of modernising our gas transport system at around $1.5bn. We have secured funding from the ADB for part of the project, and we also plan to work with the European Bank for Reconstruction and Development, World Bank and Japanese public sector funds.

GM: What are the biggest challenges you face?
SU: One of the hardest tasks is to change our corporate culture and mindset of our employees. We have brought in external consultants to help with this and they are currently conducting training to bring our staff up to international standards.

Another major project is the digitalisation of our operations. We need to integrate all our processes, from pipelines to compressor stations, in one platform. This will hugely improve the efficiency of our operations. We are working closely with our strategic partner, Gazprom, in this area.

Our other main challenge is to improve our gas storage facilities. In our region, levels of gas consumption are very different in winter and summer. We need to be able to store gas produced during the summer period so that we can meet customers’ requirements and increase exports in winter.

We have a large underground gas storage facility at Gazli, one of Uzbekistan’s largest gas fields. We have set up a joint venture with Forus JSC, a Russian company, to reconstruct the storage facility. This will more than triple the gas storage capacity to 10 billion cubic metres.

Work is already underway on the first phase of the project, which will double the storage capacity to six billion cubic metres by the end of 2021. The second phase is due to be completed in 2024. Infrastructure at the facility will be modernised in parallel with the reconstruction work.

The total cost of the project, which also includes additional exploration and development of the gas and oil fields at Gazli, is $850m.

GM: Is Uztransgaz ready for projected increases in gas production?
SU: We are working closely with Uzneftegaz and are confident that we will be able to cope with the expected increase in production. Part of this will obviously be supplied to the internal market, where we are expecting a steady rise in demand in line with the growth of the Uzbek economy.

We are also ready to support the planned increase in exports. Uzbekistan is located on two main gas transit corridors. One runs from Turkmenistan via Kazakhstan to Russia, while the other connects Turkmenistan to China.

We currently supply around eight billion cubic metres of gas to China but have the capacity to increase that by a further 25%. In future, we want to utilise to the maximum all our export capacity.
Powering up Uzbekistan’s electricity supply

A radical restructuring and upgrading of Uzbekistan’s power sector is creating opportunities for foreign investors and adding new generation sources, from renewables to nuclear

By Lucy Fitzgeorge-Parker

The restructuring of Uzbekistan’s energy industry has been mirrored in its power sector, where policymakers have embarked on a radical programme of reforms to increase capacity and attract foreign investment.

The country’s power complex has traditionally struggled to meet the demands of a rapidly growing population and developing economy due to outdated infrastructure and inefficient management.

With consumption forecast to surge over the coming years, as economic reforms spur a jump in industrial production, the need for change has become urgent.

“We are seeing new industries coming on line in processing, textiles, agriculture, manufacturing and metallurgy; as well as a huge expansion in tourism and other services,” says Jurabek Mirzamahmudov, first deputy minister of energy. “All of these will need access to a stable and reliable electricity supply.”

Meeting this demand will not come cheap. Over the next five years, officials estimate that more than $2.8bn will be required to upgrade existing infrastructure, while adding new power generation could cost as much as $14.4bn.

“The aim is to create a modern, highly efficient electric power complex based on the use of advanced world experience to create an optimal, economically sound structure of generating capacities and electric grid facilities,” says Fayzulla Shaismatov, deputy chairman of Thermal Power Plants.

To reduce the drain on the state budget, as well as enhance the flow of technology and know-how into the country, the government is looking to attract foreign investors to a sector that until recently was largely off-limits to outsiders.

“We have never had private sector investment in our power generation or distribution network, so this is a huge opportunity,” says Mirzamahmudov. “And on the first come, first served principle, those who get in earliest will benefit the most.”

The key step in the opening up of the sector was taken in March, when a decree by President Shavkat Mirziyoyev ordered the break-up of Uzbekenergo, Uzbekistan’s notoriously inefficient state-owned electricity giant.

Previously, the firm was responsible for the production, transmission, trade and distribution of nearly all Uzbekistan’s electricity.

The new structure, devised in collaboration with international financial institutions (IFIs) including the World Bank and Asian Development Bank (ADB), splits these roles between three new joint stock companies.

Responsibility for electricity generation has been assigned to Thermal Power Plants. National Electric Networks of Uzbekistan now oversees transmission and trade, including imports and exports, while Regional Electric Networks distributes and markets electricity to end users.

“We want to introduce modern corporate governance into all three companies,” says Mirzamahmudov. “We are in discussions with IFIs to bring in foreign experts, not only as consultants but also potentially as senior managers.”

“We also plan to move all the companies to IFRS reporting standards to improve transparency.”

At Thermal Power Plants (TPP), these changes will apply not only to the company itself but also to its subsidiaries. The firm, which last year generated 90% of Uzbekistan’s electricity, controls 10 power plants across the country. Most are gas-powered, although two in the Tashkent region use coal.

Under the new system, these plants have also been restructured as joint stock companies with their own supervisory boards and independent directors, with TPP effectively acting as a holding company, as part of the preparation for a planned programme of privatisations.

A pilot deal is already in the works. In March, during a visit by President Mirziyoyev to the United Arab Emirates, Abu Dhabi-based investment company Mubadala agreed to start negotiations to take a stake of at least 50% in the Talimarjan thermal power plant in Kashkadarya province.

The plant has already been expanded in recent years with the addition of two combined-cycle plants with a total capacity of 900MW constructed by Daewoo and Hyundai.

A second project is underway to build another two combined cycle gas turbines (CCGTs) with a capacity of at least 900MW, with $790m of financing backing from the ADB and European Bank for Reconstruction and Development.

Further privatisations of existing power plants are scheduled to follow. In the meantime, investors keen to gain access to the sector also have the option of getting involved in greenfield projects.

Work is already underway on the construction of two combined cycle gas turbine plants by Turkish companies in the Sirdaryo and Tashkent regions, and in September Saudi Arabia’s ACWA Power signed an agreement with the Ministry of Energy to build two power plants with a total capacity of 2,250MW.

RENEWABLE ENERGY TO THE FORE

One of the plants will be gas-fired but the other will utilise wind power, as part of an ambitious plan by the Uzbek government to build renewable energy capacity.

“We have large reserves of natural gas but like any resource that will deplete over time,” says Mirzamahmudov. “That’s why we are actively working to introduce new power generation sources, as well as increasing the efficiency of existing plants, in order to reduce gas consumption.”

At present, Uzbekistan has a total installed capacity of 11.2GW. Policymakers are aiming to triple that by 2030, with nearly half of new capacity coming from renewable sources.

Part of this increase will come from hydroelectric power. Currently Uzbekistan’s only renewable energy source, the government is aiming to double its share in the country’s energy mix over the next 10 years to around 13%.

The remainder of the renewable energy quota — and a fifth of total electricity generated in Uzbekistan — will be provided by new solar and wind power installations.

A survey by the Uzbek government, in conjunction with the ADB, shows high potential for solar power
POWER SECTOR

Investment highlights: electricity

The modernisation and upgrade of 22 main power substations in Uzbekistan
- Starting date: 2017
- Finish date: 2022
- Finances: World Bank’s loan: $150m
- The total cost of the project: $292m

The construction of the Tahkhiatash-Sarimov transmission line in the Khorezm region
- A 340 km stretch of line
- The total cost of the project: $258mn
- $150m by the Asian Development Bank (ADB)
- Finishing date: 2019

An overhead transmission line from Navoiy TPP to Bespan
- The total cost of the project: $80m, partly funded by the European Bank for Reconstruction and Development (EBRD)
- Electricity for the newly established mining and metallurgical production facilities in the Navoiy region and to develop the power grid in the northwest

A high-quality power supply to the Tashkent Metallurgical Plant Construction of Pulii Khuuri (Hoja-Alvon) power line
- The total length of the line is 245.6km, of which 45km runs through the Surkhordaryo region and 200.6km through Afghanistan

new installations in the Karakalpakstan region.

Mirzamahmudov notes that adding renewable energy capacity will also require the expansion of Uzbekistan’s gas-fired power network. “We will need additional capacity to regulate supply and ensure sufficient reserves,” he says.

New gas-fired power plants will be overseen by a new department of the Ministry of Energy, created in August by presidential decree, which has been tasked with co-ordinating and overseeing the development of energy-efficient technologies.

“This unit has the responsibility of ensuring that new CCGTs are built to maximise efficiency and reduce the consumption of gas,” says Mirzamahmudov.

For nuclear power, meanwhile, policymakers looked closer to home for help. Uzbekistan signed an intergovernmental agreement with Russia in September 2018 for the development of the country’s first nuclear power plant.

The facility, which will be constructed by Russian state-owned giant Rosatom, will have two blocks with a combined capacity of 2.4GW. The first is due to come on line in 2028 and the second in 2030.

“We want to add nuclear power as well as renewables to ensure the sustainability of our energy mix,” says Mirzamahmudov. “With nuclear, you can plan your energy strategy for the next 60 years — and we are one of the top countries in the world for uranium production, so we have the raw material.”

TARIFF REDUCTIONS

For all current and potential investors in Uzbekistan’s electricity generation sector, one of the key issues will clearly be the future direction of tariffs.

Traditionally, electricity prices have been heavily subsidised by the state but President Mirziyoyev’s government has undertaken to introduce market mechanisms. A rise in tariffs was implemented in August and further increases are promised.

“This will be a sensitive issue, because tariffs are not only a mechanism to attract investors but also have a high social impact,” says Ergashevich.

“To protect the population, the government has therefore decided to implement gradual increases in tariffs.

“Nevertheless, we have a strong understanding that tariffs should be cost-covering.”

Following the unbundling of Uzbekenergo, each power plant in Uzbekistan will now negotiate tariffs separately with the monopoly purchaser, National Electric Networks.

The company, which is scheduled to remain in state ownership, is also responsible for co-ordinating cross-border electricity trade and transmission.

At present, Uzbekistan imports electricity from neighbouring countries including Kyrgyzstan, Tajikistan, Kazakhstan and — since last year — Turkmenistan.

“We are trying not to utilise older generation units that are not energy efficient so we are not running at 100% of our installed capacity,” says Mirzamahmudov.

“We have therefore enhanced regional co-operation in this area in order to meet increasing demand.”

At the same time, Uzbekistan is also looking to step up exports of electricity to Afghanistan. The country has been selling electricity to its southern neighbour since 2002 and last year delivered 2.6bn kWh.

National Electric Networks is now working on a new 154km transmission line to Afghanistan. The Uzbek government has agreed to provide a discount for the construction of the line in return for a 10-year contract from the Afghan purchaser, a condition set by the ADB for the provision of project finance.

REGIONAL DISTRIBUTION

The final pillar of Uzbekistan’s new power complex is Regional Electric Networks, which is responsible for delivering electricity to end users.

The company comprises 14 regional electric power networks, which supply around 300,000 Uzbek businesses and seven million households. Individual and communal domestic consumption accounts for 35% of the total, with industry and agriculture taking a further 41% and 20% respectively.

As with the other parts of Uzbekistan’s power network, the lines and facilities operated by Regional Electric Networks are severely outdated. The company estimates that around 58% of all types of overhead power transmission lines require modernisation and one-third of all substations.

“More than 5% of the elements of distribution power networks are operated with a period of more than 30 years and have practically exhausted their resources,” says a company spokesperson.

“The deterioration of power lines and transformer units means there will be a problem with the supply of electricity in the near future. As well as modernising existing infrastructure, we urgently need to commission new facilities.”

Under the new power sector strategy, Regional Electric Networks has been tasked with constructing and reconstructing at least 15,000km-17,000km of transmission lines and 450 transformer substations annually for the next 10 years.

The company is also implementing a new automatic system for the commercial accounting of power consumption to reduce loss and theft of electricity, improve collection of revenues, and allow remote power connection and disconnection.

“After the implementation of the project, the share of average commercial losses from the total forecast losses will decrease from 12.5% to 5.0%,” says a company spokesperson.

The total cost of Regional Electric Networks’ expansion and modernisation programme is estimated at $1.7bn over the next 10 years.

Again, the government is looking to source some of this from foreign investors. “We want to bring in private sector investment, including from outside Uzbekistan,” says Mirzamahmudov. “We are also considering privatisation as an option.”

in the south of the country, especially in the Surxondaryo region, as well as in the Fergana Valley. For wind power, the most promising regions are Navoiy, Bukhara and Karakalpakstan.

The majority of new capacity will come from solar power, which is expected to provide 5GW of installed capacity by 2030. Wind power will account for a further 3GW. All of these new facilities are scheduled to be built by foreign investors through public-private partnerships.

Initial indications suggest that interest in the sector will be intense. A pilot 100MW solar power plant project in the Navoiy region, developed with the support of the International Finance Corporation, attracted expressions of interest from 24 firms, of which 11 qualified for the second phase of the tender.

IFIs have also backed wind power initiatives, including a 0.75MW pilot project near Lake Charvak in the Tashkent region and feasibility studies for
POWERING UZBEKISTAN’S NEW ENERGY STRATEGY

**GlobalMarkets: What has the government’s new energy strategy meant for Thermal Power Plants?**

**Fayzulla Shaismatov:** The biggest change in our company has been the attitude to efficiency. Uzbelenergo was a large and cumbersome vertically integrated company. It was very difficult to identify bottlenecks because financing was centralised. The inefficient parts of the business were covered by the more efficient, mainly through income generated from the sale and export of electricity.

After unbundling, we know what our weak spots are and where we need to focus our efforts to minimise the costs of production and to improve the management efficiency of our power plants.

We are working to implement modern management principles in all our entities, and we are very focused on corporate governance and transparency. We are introducing supervisory boards with independent members in our power plants.

We want to do this and we have to do it, because we currently rely heavily on international financial institutions (IFIs) for financing, and their requirements on transparency and efficiency are very stringent. They also set high standards for us in terms of environmental impact.

**GM:** What has changed for the power plants?

**FS:** Every plant now has a power purchase agreement with National Electric Grid. The cashflow goes directly to the plant and the management can decide how to use the money.

This was done to create a sense of asset ownership and economic incentives. Previously nobody cared about efficiency because they received funding from the parent company on demand.

Now each power plant has started to make a more accurate assessment of their costs, look for bottlenecks and weak spots, and work on improving them.

There is still long way to go but we have already achieved a shift in attitudes. The managers of the power plants now know their income is dependent on how efficiently they work. They are the masters of their own businesses.

**GM:** How much investment do you need over the next 10 years?

**FS:** According to forecasts for demand growth, we need to at least double our existing capacity, which will require a considerable amount of investment.

Unfortunately around 80% of our generating units are outdated and obsolete, with an average age of more than 30 years, so we also have to decommission most of the existing units.

This means the pace of renovation has to be very rapid, which is why the government wants to open the door to private investment. Attraction of private investment is set to be the primary goal because the government has realised that it is too heavy a burden for them to bear alone.

**GM:** What are the main challenges you face today?

**FS:** Our biggest challenge is to increase efficiency. Once private investors start building independent power producers (IPPs) it will become an existential matter for us, because we will have to compete in the open market against firms with the most advanced technology and management systems.

It will take two to three years for new investors to construct and commission their power plants, so that’s how long we have to structure our operation to become competitive enough to survive.

Another major challenge is changing the attitude of our staff. After many years working under the old management system it’s difficult to break the inertia in their minds and switch them to a “business oriented” mode.

Fortunately, we have very strong support from IFIs including the World Bank, European Bank for Reconstruction and Development (EBRD) and Asian Development Bank (ADB). They are helping a lot by running seminars and providing access to consultants in this sector.

We are trying to ensure that we meet the highest standards in corporate governance, and in parallel to educate our employees. We are running courses on topics including corporate governance and project finance in order to build capacity in our workforce.

We also want to bring more international managers into the company. With the help of the IFIs, we are currently looking outside Uzbekistan for a new deputy chairman, who will be responsible for adopting international standards of expertise, governance and management.

**GM:** How important is knowledge transfer?

**FS:** It is the number one priority for us at the moment. Most of our fleet of generation units are obsolete, and new units need experienced people who are educated to work on these units efficiently. It’s not enough to buy new equipment—you need people who can operate it.

We are also aware that green technologies are very much in focus at the moment and that we need to keep up with this trend. We are paying a lot of attention to energy-saving technologies.

**GM:** Would you consider raising funds through the capital markets?

**FS:** To develop further and expand our company we will need access to capital markets, but first we need to complete the process of becoming self-sustainable.

Cost-covering tariffs were only introduced in August. It will take a couple of years at least to get on a solid footing after that, because to access the capital markets you have to be strong enough to persuade your counterparts to lend you money.

At the moment we rely heavily on state support, but the government has made it clear that in future this will be reduced and we will have to take care of ourselves. So first we need to achieve self-sufficiency, then in two or three years we will be ready to get an international credit rating and enter the capital markets.

*“First we need to achieve self-sufficiency, then in two or three years we will be ready to get an international credit rating and enter the capital markets.”*
Currently, our organisation consists of 14 regional power transmission lines and 77 substations. Overall, 4,713 specialists work in the company.

GM: What are the main challenges you face?  
EK: The total length of Uzbekistan’s power grid is around 255,000 km, more than six times the length of the Equator. Among them, 9,700 km is 220-500 kV main overhead power transmission lines which are serviced by our organisation. It is clear that such a long network needs constant construction and repair, modernisation and innovative technologies.

Unfortunately, nearly 62% of our electric network is more than 30-35 years old. The distribution networks are extremely worn out, which leads to a large loss of electricity, now accounting for more than 2.8% of the total energy supplied by thermal power plants to the grid.

GM: What are your main investment projects?  
EK: The largest project we are working on at the moment is the modernisation and upgrade of our 22 main power substations in order to increase the reliability of electricity supply. This involves the renewal of old machinery and power lines with modern equipment corresponding to international standards.

The renovation project was started in 2017 and will finish in 2022. It is being partly financed by the World Bank, which has provided a loan of $150m. The total cost of the project is $292m.

Also ongoing is the construction of the Takhlatash-Sarimoy transmission line in the Khorazm region. A 340km stretch of line is being built at a cost of $258m, of which $150m has been provided by the Asian Development Bank (ADB). The project is due to be completed this year.

Work also began this year on the construction of an overhead transmission line from Navoiy TPP to Besopan. The new line, which will cost $80m and is partly funded by the European Bank for Reconstruction and Development, will provide electricity for the newly established mining and metallurgical production facilities in the Navoiy region and to develop the power grid in the northwest.

Our next major project, which will start this year, will be in the Tashkent region. We have undertaken to provide a high-quality power supply to the Tashkent Metallurgical Plant, as well as to meet the needs of the population and industrial facilities in Tashkent and the border areas of Tashkent region.

GM: Do you have any projects outside the country?  
EK: Yes, we are currently working on the construction of the 500kV Surkhon-Puli-Khumri power transmission line to Afghanistan.

This will improve our relations with Afghanistan and enhance our ability to export electricity to neighbouring regions, thereby increasing the inflow of foreign currency into Uzbekistan and our standing in the international arena.

The total length of the line is 246 km, of which 45 km pass through the Surkhandarya region of Uzbekistan and 200 km through Afghanistan.

GM: What effect have improvements in regional co-operation had on your work?  
EK: In the last three years, we have seen dramatic change. Previously, working on our transmission lines outside Uzbekistan was very challenging due to the difficulty of moving equipment and personnel across borders.

Today, thanks to the efforts of our president, this has become much easier. We have been able to monitor and make repairs to our lines in Tajikistan, Kazakhstan and Turkmenistan, and our regional partners have been able to come and work in Uzbekistan. This has been mutually beneficial.

GM: Are you ready to support the expansion of renewable energy in Uzbekistan?  
EK: It is very important for us to be prepared for the transmission of generated electricity by renewable energy sources.

As a company, we are very supportive of initiatives to produce cleaner energy and improve efficiency. We are working on bringing the issues of energy efficiency and energy conservation to the general public and introducing proposals to start education on the topic at pre-school age.

We also closely work with citizens, raising awareness about what steps must be gone through to produce electricity, how it can be delivered, and the continuous and quality distribution of energy to consumers. Energy efficiency and efficient use of natural resources are inseparably linked with the development of society. I think this is our duty to the future generation and our debt to nature.

GM: What other changes are you making at National Power Networks?  
EK: We are making gradual changes to our company management, partly as a result of the projects we are working on. New technologies require a different approach to planning and forecasting, so this is helping us to change our management patterns.

We are also working with IFIs to improve our internal standards. We recently undertook a project with the ADB on upgrading our information communication technologies.

We also understand that we need to bring in expertise and technology from outside Uzbekistan in order to build a modern transmission network.

We are open to innovation and keen to work with foreign partners with experience in the energy sector, and hope we can provide a platform for mutually beneficial cooperation.
Uzbek chemicals sector unveils formula for growth

Policymakers have unveiled an ambitious plan to revitalize and expand Uzbekistan's chemicals industry with the help of foreign investors to serve booming domestic demand and boost exports

By Lucy Fitzgeorge-Parker

For a country rich in hydrocarbons and boasting a large domestic market, Uzbekistan has traditionally underperformed when it comes to the production of chemicals.

The industry currently accounts for just 2% of the country's total production volume and 1% of GDP. "These are very small numbers," says Temirov Odil, chairman of local chemicals company Uzbekmosanoat. "For developed countries the figure is more than 10%.

Uzbekistan's reformers are aiming to close that gap. The process began two years ago when President Shavkat Mirziyoyev ended the practice of price-setting by the government for chemical products, allowing the sector to move to market principles.

The next step was a year-long analysis of the Uzbek chemical industry, undertaken in conjunction with Boston Consulting Group, to assess market demand and identify key areas for investment.

The results of this study were released in April, when the government unveiled an ambitious $12bn strategy to modernise and restructure the sector with the help of foreign investors.

The primary objective of the programme, which comprises more than 30 projects to be completed by 2030, is to reduce Uzbekistan's dependence on imported chemicals and service rapidly growing domestic demand.

"We are a developing country with a population of 32 million and economic growth of around 5% per annum," says Odil. "We can expect a big increase in demand for all basic chemical products."

A core plank of the strategy — which aims to increase chemicals production to 5% of GDP — is the expansion of Uzbekistan's organic chemicals industry.

Despite its ample reserves of natural gas, the organic chemicals segment currently accounts for just 11% of the country's chemical output. By 2030, this is scheduled to increase to at least 50%.

Much of this growth is due to come from the manufacture of new value-added polymer products including polyethylene terephthalate (PET), polystyrene, butyl acrylate and others.

This in turn will support some of Uzbekistan's largest and fastest-growing industries. The country's textile sector last year imported around 70,000 tonnes of PET fibre, while more than 85,000 tonnes of PVC was purchased from foreign suppliers by Uzbek textile and processing companies.

Household chemicals are also largely sourced from outside the country. Around 30,000 tonnes of linear alkylbenzene (LAB) and linear alkylbenzene sulfonic acid (LABSA) are imported annually for detergents and other household products.

Part of this domestic demand will in future be met directly by Uzbekmosanoat, Uzbekistan's largest state-owned chemical producer. The firm has announced plans to start production of PVC at its flagship Navoiyazot complex. Initially, a new facility will produce 100,000 tonnes a year of the PVC polymer.

"According to our forecasts that will not be enough to keep up with increasing in-country consumption, so we will subsequently add a second complex with a capacity of 130,000 tonnes," says Odil.

Uzbekmosanoat also plans to begin production of LAB and LABSA using feedstock from the Shurtan gas chemical complex and a new gas-to-liquid (GTL) complex due to be created by state oil and gas giant Uzbekneftegaz.

"We will produce enough LAB and LABSA to cover full in-country consumption," says Odil. "We also expect to be able to export around 20,000 tonnes a year of household chemicals to nearby countries."

Overall, policymakers expect domestic demand to account for around two-thirds of Uzbekistan's output of organic chemicals by 2030, with the rest being sold outside the country.

The sector development programme also calls for a step-up in output of other chemicals currently produced by Uzbekmosanoat.

These include drilling and water system chemicals for the Uzbek oil and gas and petrochemicals industry, as well as adhesives and melamine for the wood processing and furniture sectors.

FERTILISING GROWTH

Uzbekmosanoat also manufactures a range of chemicals including cyanic salts and urea for major mining and metallurgical combines based in Almalyk and Navoiy, respectively Uzbekistan's leading producers of non-ferrous metals — copper and gold — and uranium.

Production of mineral fertilisers, which currently account for around 75% of Uzbekmosanoat's total chemical output, will also remain a key component of the government's strategy for the sector.

Indeed, policymakers see the segment as offering excellent opportunities for export growth. "There is strong demand for mineral fertilisers in other Central Asian countries, Turkey and Ukraine, as well as China, India and southeast Asia," says Odil.

Despite being a landlocked country, Uzbekistan has good road and rail links to Afghanistan, Tajikistan, southern Kazakhstan and Russia. The government is also backing the development of a rail link to China.

Along with the large and growing domestic market, this export potential is expected to be one of the main attractions of the Uzbek chemical industry for foreign investors, who will have the chance to gain exposure to some of the country's key assets over the next four to five years.

April's presidential decree mandated the privatisation of a clutch of production facilities and non-core assets under the control of Uzbekmosanoat. The company, which employs 33,000 staff, currently comprises 14 industrial enterprises and six service organisations.

Topping the list of assets for sale are three fertilisers and chemical plants: the Dekhkonobod potassium plant, Ferganaazot, which produces nitrogen fertiliser; and the Kungrad soda plant.

The Uzbek government is offering to sell a 51%
share in each of the three, in return for investor commitments to modernise facilities, increase capacity — by more than 100%, in the case of the Kungrad soda plant — and establish new production lines.

All three are profitable, although a fall in global potassium prices has recently affected revenues at Deykkonobod. The most profitable of the three is Perganazot, which boasts an Ebitda margin of around 40%.

The privatisation process is already underway, with EY acting as investment consultant to Uzkinmosanot. More than 150 investors have been invited to view the privatisation process and more than 20 have expressed an interest in Deykkonobod, while the other facilities have each attracted half a dozen potential buyers.

“With big projects, naturally the risks are also big,” he says. “Investors are therefore keen to partner with local entities that own the mineral resources, feedstock and infrastructure.”

**ECONOMIC ZONES**

Policymakers have also provided assurances to foreign direct investors regarding the provision of utilities, while further benefits will come from a new drive by the Ministry of Economy and Production to promote co-operation between sectors within Uzbekistan.

To encourage the creation of industry clusters, the government has created a series of economic zones across the country, including one comprising the whole of the Navoiy region.

Other greenfield opportunities up for grabs include Samarkandkimyo, where the government is offering to sell 100% of the company in return for a commitment by the buyer to build a new production facility for phosphoric acid and NPK fertilisers.

The proceeds from these privatisations will be put into an investment fund, which will be used to finance Uzkinmosanot’s part of the development programme.

Part of this funding will be spent on knowledge transfer. “For each new project, we will sign licensing agreements to bring in technology and know-how,” says Odil. “We are also planning to send our specialists abroad for training, as well as bringing experts here to provide in-country training.”

This will be backed by a drive to improve technical education in Uzbekistan’s universities. This year will see the opening in Tashkent of a branch of Russia’s Mendeleev University of Chemical Technology, the result of a collaboration between Uzkinmosanot and the Ministry of Higher and Secondary Education.

The company is also working on a project to create a research and development centre in Uzbekistan for the chemicals industry. A feasibility study funded by Korea Eximbank is already underway and officials say the centre could open as early as 2023.

“This will be an invaluable resource to ensure we have the expertise in Uzbekistan to drive our industry forward,” says Odil.

Meanwhile, Uzkinmosanot is also undergoing a major internal restructuring to improve corporate governance and transparency.

The resolution passed in April mandated the appointment of independent directors to the firm’s supervisory board and the establishment of an audit committee, as well as the preparation of financial statements according to IFRS accounting standards.

Significant progress has already been made. IFRS standards have been introduced at the entities earmarked for privatisation, while the parent company is due to follow suit shortly.

This in turn will pave the way for Uzkinmosanot to obtain an international credit rating and, in the near future, access the Eurobond market.

Odil notes, however, that bond buyers will have to wait to gain exposure to the company. “First we have to sell our shares in the main entities listed for privatisation, which will increase our attractiveness for foreign investment,” he says.

In the meantime, the firm is looking to attract finance from international public and private sector banks for individual projects.

“One of the reasons for creating joint ventures with the direct involvement of foreign investors is to bring in project financing from the likes of Export-Import Bank of China and Japan Bank for International Cooperation, and from others ECAs,” says Odil.

There are no plans at present to sell equity stakes in Uzkinmosanot, although Odil says that will come further down the line. “Naturally in future the government will look to reduce its participation in the company,” he says.
PPP BRINGS KNOW-HOW AND EXPERTISE INTO THE COUNTRY

In an interview with *GlobalMarkets*, Golib Kholjigitov, head of Uzbekistan’s PPP Development Agency, lays out the advantages that working with the private sector can bring in terms of lower costs and more efficient delivery of much-needed infrastructure projects.

The government also wants to improve the financial sustainability of the sector. Over the past decade, high levels of energy subsidies meant that our energy companies were loss-making and incurred debts.

Demand for electricity in Uzbekistan is forecast to grow by 40%-70% over the next 10 years, so it is clear that considerable investment is needed in the power sector. We estimate the figure at around $15bn.

**GM**: What are the advantages of the PPP format?

**GK**: Given the level of investment required, the government is keen to leverage private sector funding to solve public sector issues such as the contingent-liability structure. With PPP, most of the risks are taken by the private sector, from market risk to operational risk.

We also know from experience in other jurisdictions that the cost overrun on PPPs is nearly three times lower than on projects using traditional procurement.

Similarly, PPP projects tend to be delivered in a more timely manner and to a higher standard, because deadlines and key performance indicators are built into the contracts and power purchasing agreements. These are powerful motivating factors for private companies.

The other big advantage of PPP is that it brings know-how and expertise into the country. Foreign companies will not just be responsible for building assets but also for operating them, maintaining them and managing them to international standards — which is exactly what our country needs.

**GM**: Which sectors are you focusing on?

**GK**: We have several priority areas, including energy, transportation, water, healthcare, agriculture and education.

The energy sector is particularly important for us. It provides the foundation for any economic growth and the current technology is quite outdated, with low efficiency and instability in some areas. We are therefore very focused on encouraging investment in electricity generation and distribution.

We want to support the government’s strategic plan for the development of the energy sector. This includes the diversification of our energy capacity with a focus on renewables and the modernisation of outdated infrastructure.