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ESG PRINCIPLES AS A TOOL FOR INCREASING THE SUSTAINABILITY OF UZBEKISTAN'S ECONOMY

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Abstract

The article describes the emergence of the foundations of ESG principles in world practice and their implementation in Uzbekistan's economy. Also, for a more in-depth study of these criteria, the authors used PESTEL analysis of the construction industry and company.

Keywords: ESG criteria, PESTEL analysis, legal framework, green economy.

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Introduction

In the modern world, people are faced with acute environmental problems. Society and governments have already recognized the importance of a sustainable and environmentally oriented economy. Social and environmental problems such as population growth, climate change, pollution and water and air shortages threaten infrastructure and economic development. Today, the green economy, as a new form of economics, is primarily focused on environmental sustainability, social justice and economic growth. The main idea is a balance between the needs of society and the preservation of the environment.

President Sh.M. Mirziyoyev, in his speech at the ceremony dedicated to the 32nd anniversary of the independence of the Republic of Uzbekistan, noted that environmental problems and the associated water shortage are important. If on one side of the scale is the need to develop construction, industry, and agriculture, then on the other are the most important issues for each of us: water conservation, prevention of environmental pollution and rational use of land resources. The government's task is to maintain a balance of both directions. Natural resources must be used wisely, thinking not only about today, but also about tomorrow¹.

In this direction, an accelerated transition to an economy based on careful use of water, energy and other natural resources is of great importance. The task of creating

¹ Speech by the President of the Republic of Uzbekistan Shavkat Mirziyoyev at the ceremony dedicated to the 32nd anniversary of the independence of the Republic of Uzbekistan, 08/31/2023.

<https://president.uz/ru/lists/view/6637>

“green” and digital technologies and innovative production enterprises is also relevant for us.

ESG (environmental, social and governance) criteria have become important tools for improving environmental and social conditions and increasing the sustainability of enterprises. Recently, the construction industry has also been increasingly focused on applying ESG principles to reduce the negative environmental impact of construction activities and ensure the sustainable development of the construction industry as a whole.

ESG is a set of characteristics of company management, which achieves the involvement of this company in solving social problems, including problems of implementing a “green economy”, problems of reducing social inequality, opacity of business, low social responsibility [2].

Methodology

The study of ESG criteria, which evaluate the environmental, social and governance performance of companies, can be carried out using various scientific methodologies. Comparative analysis is a method of studying and comparing two or more objects, phenomena, processes or data in order to identify differences, similarities and features between them.

Results

The author has studied the history of the emergence of the ESG acronym. A comparative analysis of foreign literature and leading publications on this topic was carried out. An analysis of the current legal framework for the implementation of ESG principles in the Republic of Uzbekistan was carried out. Also, the authors used the PESTEL analysis tool to analyze the activities of the industry and the company, which made it possible to identify the most significant factors.

Analysis

The concept of ESG has existed and been discussed since the 19th century, but in recent years this area has become so popular that the amount of assets under management of responsible investment funds has reached \$31 trillion, according to estimates by the Global Sustainable Investment Alliance[3].

For the first time in its modern form, the principles of environmental, social and corporate governance (Environmental, Social and Governance) were institutionalized by UN Secretary General Kofi Annan in 2004, when he approached the CEOs of the world's largest companies with a proposal, under the auspices of the IMF, to include these principles in their strategies. The appeal was called Who Cares Wins. The fight against climate change is one of the UN sustainable development goals. Undoubtedly important, but not the only one. For one simple reason - today it is non-compliance with the principles of the environmental agenda that leads to a tangible financial effect [4].

In 2005, the term ESG gained wider acceptance when the UN supported the Principles of Responsible Investment (PRI) initiative. This document called on investors to consider ESG criteria when making decisions [5].

After 2010, demand for responsible investing began to emerge, which led to the emergence of a whole category of social investors. Credit ratings have become complemented by ratings or labelling of issuers according to ESG criteria. The evolutionary process took more than 15 years: from the formulation of criteria, labeling of issuers, the

emergence of ESG ratings and rankings, to the inclusion of ESG criteria in credit risk assessment methodologies.

The main driver for the development of risk assessment of issuers, whose policies are being transformed taking into account the sustainable development agenda and achievement of ESG criteria, was precisely the request from investors.

A study by the Global Sustainable Investment Alliance (GSIA) found that ESG-focused investments reached \$35.3 trillion in 2020, an increase of 15% over the previous 2 years [5].

The phenomenon has become popular only in the last couple of years, but has already gained a foothold abroad. According to "Tinkoff Bank" Vice President Neri Tollardo, in the near future, global funds will stop investing in companies that ignore the principles of sustainable development [6].

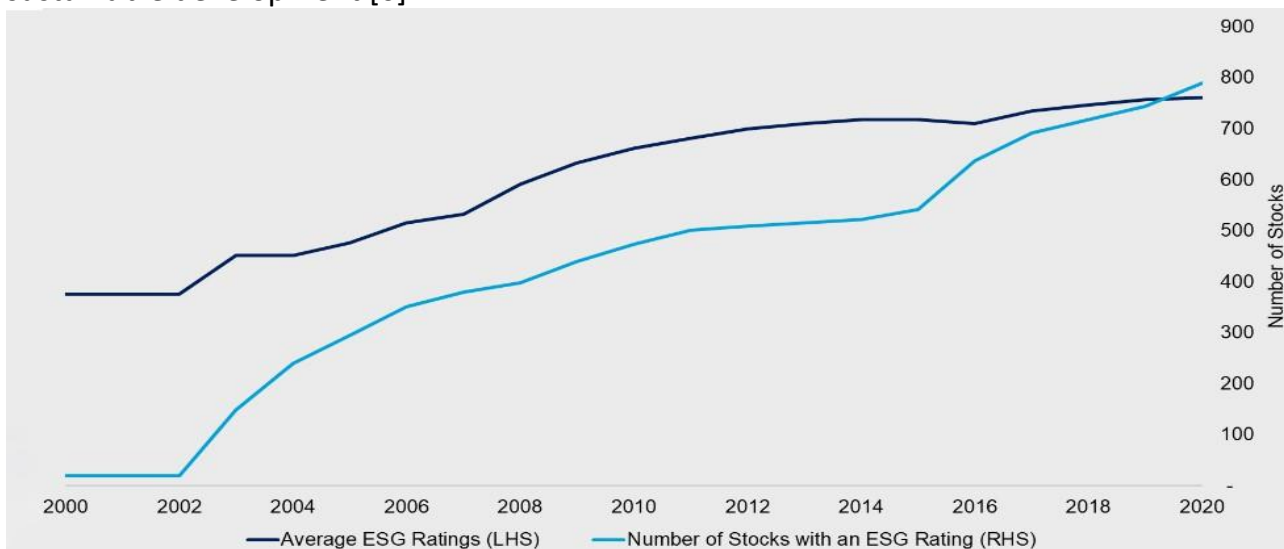


Figure 1. Number of companies with US ESG ratings and average ESG rating
(Source: Factor Research)

In the early 2000s, there were only 20 companies with ESG ratings in the United States. As can be seen in Figure 1, by 2020 their number had grown to almost 800. The average ESG rating has doubled over 20 years, which is associated with an increase in the volume, quality and availability of data [6].

According to a study by the foreign publication Bloomberg, if growth continues at the same pace, by 2025 ESG assets could exceed \$53 trillion, which is more than a third of the projected global assets of \$140.5 trillion (Figure 2) [7].

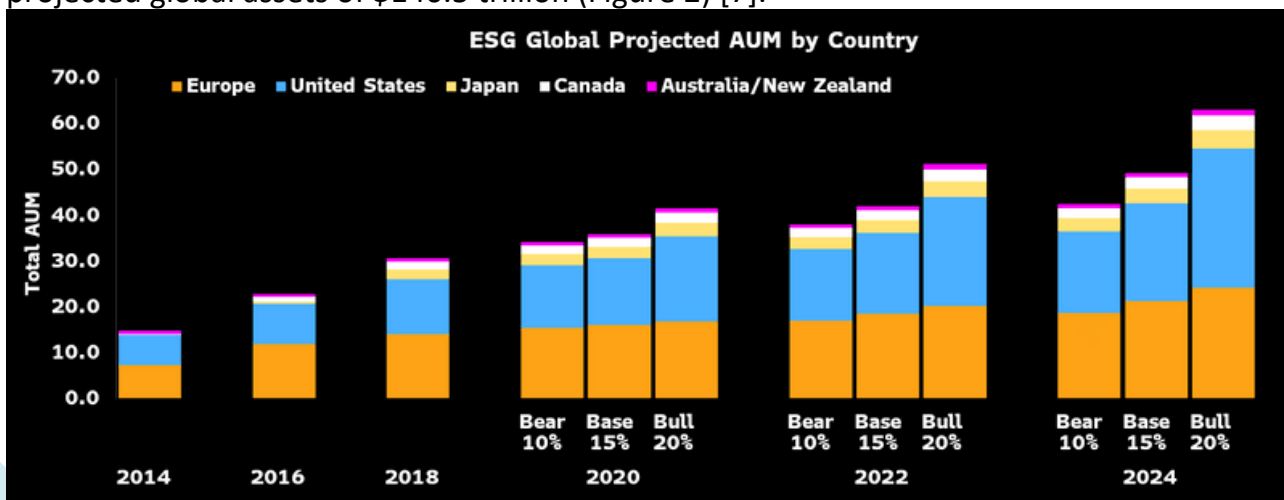


Figure 2: Projected Global ESG Asset by Country

(Source: GSIA, Bloomberg Intelligence)

In Uzbekistan, the issue of ESG factors arose after the country approved the UN Sustainable Development Goals (SDGs) in September 2015. This year, the United Nations announced the 2030 Agenda for Sustainable Development, which contained 17 interconnected goals as “a blueprint for achieving a better and more sustainable future for all.”



Figure 3. UN Sustainable Development Goals

(Source: <https://www.un.org/sustainabledevelopment/ru/sustainable-development-goals/>).

The President of the Republic of Uzbekistan Sh.M. Mirziyoyev also noted the importance and necessity of adopting a special resolution of the UN General Assembly on increasing the role of parliaments in achieving the Sustainable Development Goals and ensuring human rights. Subsequently, 17 main Goals for the country’s sustainable development until 2023 were approved on October 20, 2018 by the Resolution of the Cabinet of Ministers “On measures to implement the National goals and objectives in the field of sustainable development for the period until 2030” [8].

In recent years, the country has been undergoing a large-scale process of privatization and attracting foreign investment. Consequently, public companies are increasingly becoming interested in obtaining high ESG ratings.

Thus, in 2019, the Resolution of the President of the Republic of Uzbekistan “On approval of the Strategy for the transition of the Republic of Uzbekistan to a green economy for the period 2019-2030” was adopted [9]. The main goal of the Strategy is to achieve sustainable economic progress that contributes to social development, reduction of greenhouse gas emissions, and climate and environmental sustainability, through the integration of green economy principles into ongoing structural reforms.

To achieve the goals of the Strategy, it is necessary to implement the following main tasks [9]:

- increasing the energy efficiency of the economy and rational consumption of natural resources through technological modernization and the development of financial mechanisms;

- inclusion of “green” criteria based on advanced international standards in priority areas of public investment and expenditure;
- assistance in the implementation of pilot projects in the areas of transition to a “green” economy through the development of government incentive mechanisms, public-private partnerships and intensified cooperation with international financial institutions;
- development of a system of training and retraining of personnel related to the labor market in the “green” economy, by stimulating investment in education, strengthening cooperation with leading foreign educational institutions and research centers;
- taking measures to mitigate the negative impact of the environmental crisis in the Aral Sea region;
- strengthening international cooperation in the field of green economy, including through the conclusion of bilateral and multilateral agreements.

In the same 2019, the President signed the Decree “On approval of the concept of environmental protection of the Republic of Uzbekistan until 2030.” Within the framework of this regulatory act, in order to determine the priority directions of state policy in the field of environmental protection and ensure the achievement of National goals and objectives in the field of sustainable development, the Concept of Environmental Protection of the Republic of Uzbekistan until 2030 was approved [10].

Table 1

Uzbekistan’s development in international rankings

Ranking (Issuer)	2018	2019	2020	2020/2018
Index of Economic Freedom (The Heritage Foundation and The Wall Street Journal)	51,5 (150th)	53,3 (140th)	57,2 (114th)	+5,7 (36)
Freedom on the Net score (Freedom House)	25	26	27	+2
Ease of Doing Business (Всемирный банк)	66,3 (74th)	67,4 (76th)	69,9 (69th)	+3,6 (+5)
SDG Index (Sustainable Development Solutions Network and Bertelsmann Stiftung)	70,3 (52th)	71,1 (52th)	71,0 (66th)	+0,7 (+14)
Human Development Index (United Nations)	0,71	0,71	not published	-
Press Freedom Index (Reporters Without Borders)	60,84 (165th)	53,52 (160th)	53,07 (156th)	+7,77 (+9)
Environmental Performance Index (Yale University)	45,88 (136th)	not published	44,3 (88th)	+1,58 (+48)

(Source: <https://uzbekembassy.com.my/files/economy/bfd99d35a00424842d21e635cccd4d8b.pdf>)

The development of ESG in Uzbekistan is mainly carried out by the Ministry of Finance and the Ministry of Economic Development and Poverty Reduction. Together with the Agency for State Asset Management, the departments are responsible for accelerating the process of transition to a green economy for enterprises with state participation.

In the process of implementing measures to achieve national goals and objectives in the field of sustainable development for the period until 2030, many other departments are also involved [11].

In January 2022, the document “Development Strategy of New Uzbekistan for 2022–2026” was published. The strategy consists of seven priority areas and 100 goals that Uzbekistan intends to achieve within five years. Among these goals, there are also separate areas in the field of ESG. For example, the introduction of green principles in all areas, increasing the energy efficiency of the economy by 20%, reforming the water resources management system and others [12].

In April 2022, the President of Uzbekistan issued a decree, one of the directions of which is “accelerating the transformation and privatization of enterprises and commercial banks with state participation, stimulating an increase in qualitatively new investments and high-performance technologies, in particular based on the principles of environmental, social and corporate governance (ESG) production by reducing the share of inefficiently functioning enterprises in the economy” [13].

It should be noted that there are no requirements for mandatory disclosure of information in the field of ESG, but the Law on Atmospheric Air Protection [14] states that “enterprises, institutions and organizations whose activities are related to emissions of pollutants, biological organisms, greenhouse gases and ozone-depleting substances into the atmospheric air and the harmful effects of physical factors on it,” are obliged to “monitor compliance with the standards of maximum permissible emissions into the atmospheric air and the harmful effects of physical factors on it, keep records of them and provide statistical reporting.”

ESG risks of a non-financial nature will be subject to disclosure starting next year. New International Financial Reporting Standards will come into force in January 2024:

- □ IFRS S1 – “General requirements for the disclosure of financial information related to sustainable development”;
- □ IFRS S2 – “Climate-related disclosures”.

The application of IFRS S1 and IFRS S2 will facilitate the transition from voluntary disclosure of information related to sustainable development to a regime in which issuers will be required to disclose this information in financial statements [15].

Large companies are involved in the ESG agenda, but this activity is largely dictated by an interest in attracting additional investments rather than in meeting national regulatory requirements. The largest oil and gas company in Uzbekistan, Uzbekneftegaz JSC, has created an internal corporate ESG Responsibility Center (ESG Center). Its primary tasks are systematization and disclosure of information about activities on ESG aspects. The company was the first to publish an ESG sustainability report for 2021, which was developed with the consulting company PricewaterhouseCoopers [16]. Also, Uzbekneftegaz JSC began to develop a strategy for obtaining a rating for sustainable development from international rating agencies [17]. This experience may also be useful for other regions and joint-stock companies of the country.

As part of this study, the author conducted a PESTEL analysis of Amubukhorokanalkurilish JSC, which is located in the city of Bukhara, Bukhara region. The company, being a joint stock company, has a history of more than 50 years and is engaged in the construction of water management facilities throughout the region. PESTEL analysis includes an assessment of ESG criteria that are relevant in modern conditions.

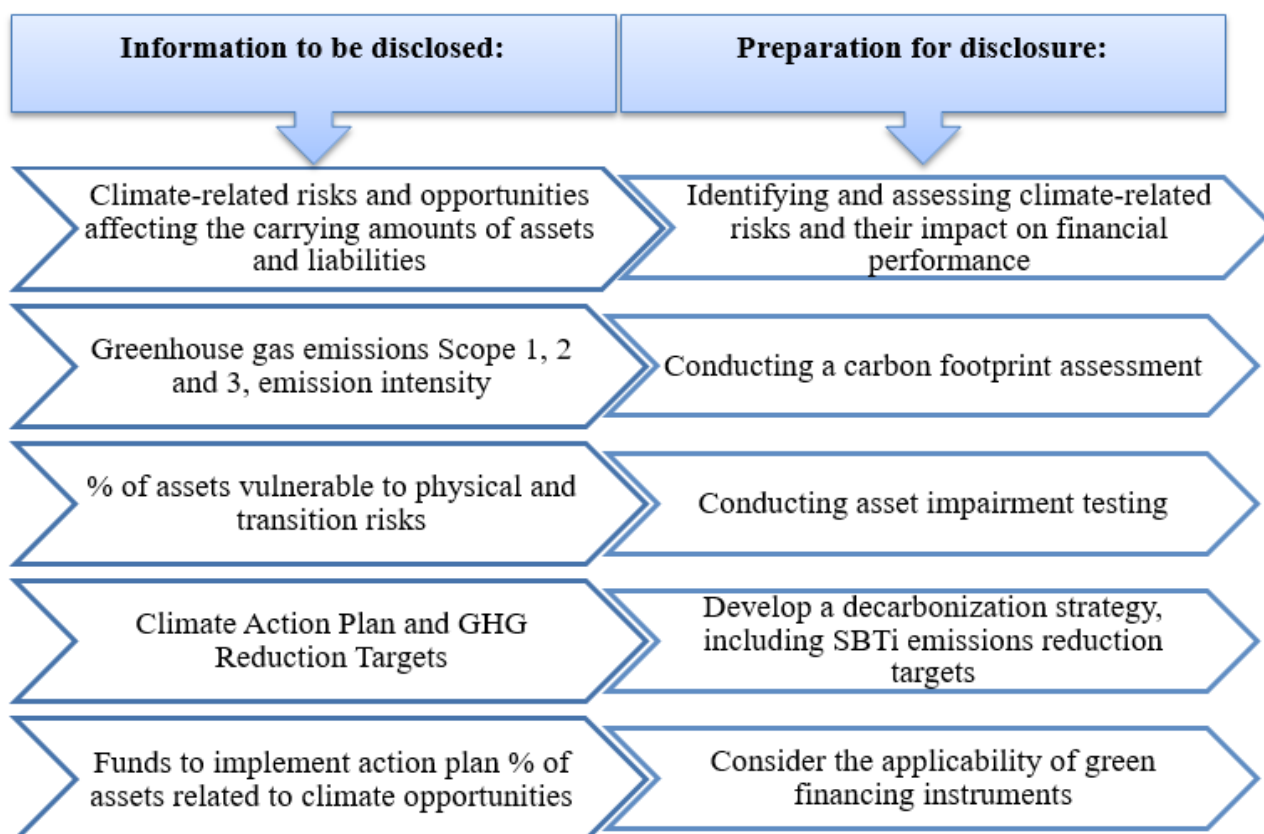


Figure 4. Information that will be contained in IFRS S1/S2 reports.

Compiled by the author on the basis of the Decree of the President of the Republic of Uzbekistan dated February 24, 2020. No. PP-4611 “On additional measures for the transition to international financial reporting standards”

Environmental legislation has a significant impact on the construction industry in the Bukhara region, requiring companies to comply with eco-standards, which leads to changes in construction processes, increased costs and stimulates the development of environmentally friendly and energy efficient technologies.

As part of this study, a PESTEL analysis was carried out, taking into account the Sustainable Development Goals and the ESG agenda. PESTEL analysis includes 6 indicators:

To conduct a PESTEL analysis, expert assessments were obtained in 6 areas from the heads of structural divisions and various levels, as well as specialists from the economic and production departments of the company.

As a result of the analysis, the most significant PESTEL factors in the activities of Amubukhorokanalkurilish JSC were identified, which have the following significance:

(P) POLITICAL - political factors

Tax policy (tariffs and benefits) 0.14

Trends towards regulation or deregulation of the industry 0.13 Bureaucratization and level of corruption 0.11

(E) ECONOMICAL - economic factors

Inflation rate and interest rates 0.15

Economic growth rate 0.14

Country's monetary and fiscal policy 0.12

(S) SOCIO-CULTURAL - socio-cultural factors

- Population growth rate 0.14
- Migration rate and immigration sentiment 0.07
- Requirements for product quality and service level 0.06
- (T) TECHNOLOGICAL - technological factors
- Level of innovation and technological development of the industry 0.11
- Development and penetration of the Internet, development of mobile devices 0.09
- Access to the latest technologies 0.06
- (L) LEGAL - legal factors
- Future and current legislation regulating the rules of work in the industry 0.15
- Tax legislation 0.14
- Antimonopoly and labor legislation 0.07
- (E) ENVIRONMENTAL OR ECOLOGICAL - environmental factors
- Environmental legislation 0.14
- Climate change, natural disasters 0.14
- Interactions with government agencies and specialized organizations of the environmental department in the field of environmental protection 0.09.

Identification of important factors in the PESTEL analysis of the construction industry of the Bukhara region allowed the author to identify likely changes that could have an impact on the company’s activities in the industry. And based on this, further develop proposals and recommendations that can help reduce the negative impact of the external environment on the activities of a construction organization.

Economic, legislative and social reforms have led to positive changes in the main indicators of investment and construction activity in the Bukhara region over the past few years. The analysis took into account the development of foreign exchange and financial markets, growing competition among construction organizations and in the process of selling finished construction products require stricter organizational and economic requirements for business entities.

The dynamics of construction and investment activity in the region showed sharp fluctuations over the studied period from 2013 to 2022 (Table 2). Periods of decline in investment in fixed assets were followed by sharp surges of growth. For example, in 2018 there was a in investment in fixed assets of -17.2%, and as a result in 2019 the volume of construction work decreased by 22% and the commissioning of residential buildings decreased by 1.5%, compared with the previous period. However, there was the largest increase in investment in fixed assets of 96.1% in 2017 and 68.5% in 2021. Also, the peak in the volume of construction work was noted at 40.8% in 2018 and 30.8% in 2021. The maximum amount of area of residential buildings that was put into operation was 1258.7 m2 in 2018 with a significant increase of 54.6% (Table 2) [18].

Table 2

Dynamics of investment and construction activities in Bukhara region (2013-2022)

	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Investments in fixed capital, billion soums	2998	3583	4075	5922	11613	9610	10366	12183	20528	21138

Commissioning of residential buildings, thousand sq.m.	683	726	787	773	814	1258	1277	1299	1337	1495,8
Volume of construction work, billion soums	1279	1648	2061	2202	2543	3581	4368	5659	7401	8340

Source: Official website of the Department of Statistics of the Bukhara Region <https://www.buxstat.uz/> and compiled by the authors based on data from this site.

Thus, over the past five years, a consistently high pace of construction work has been observed in the Bukhara region, with the exception of 2022, when this figure remained at the level of the previous year.

The above analysis suggests that the construction industry of the Bukhara region will continue to develop steadily in the future. Based on the indicators of the volume of construction work for previous periods, the author developed an optimistic forecast for 2023-2025 (Fig. 5).



Figure 5. Forecast of the volume of construction work in the Bukhara region.

Source: Official website of the Department of Statistics of the Bukhara Region <https://www.buxstat.uz/> and based on data from this site, the author predicted using MC Excel software.

In such conditions, the further development of the construction industry will depend on the ability of enterprises and organizations of various forms of ownership to be flexible, respond to changing market conditions, the ability to realize internal potential, and also meet the modern requirements of investors.

Conclusion and suggestions

Based on the results of the study, the authors believe that the relevance of ESG factors today in Uzbekistan and its regions is growing steadily which is reflected in the current legislation of the republic. To study the influence, the authors used the PESTEL analysis technique, where the most significant factors were identified. Based on the analysis, the authors propose, as a possible solution for the company

Amubukhorokanalkurilish JSC to reduce the influence of political factors, to develop and implement policies and procedures aimed at increasing the transparency and compliance of its activities with regulatory requirements.

The above analysis of the development of the region and the company in recent years shows a significant impact on the economic and social spheres, including construction. The construction industry will be sustainable if it can effectively address economic, social, technical, environmental and legal issues, taking into account global and local requirements occurring in the external environment.

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