WORLD SCIENCE PUBLISHING

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London International Monthly Conference on Multidisciplinary Research and Innovation

# THE ROLE OF FOREIGN INVESTMENT IN ACCELERATING STRUCTURAL TRANSFORMATION OF UZBEKISTAN'S ECONOMY

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https://doi.org/10.5281/zenodo.23036782

**Abstract:** This thesis examines the role of foreign investment in accelerating structural transformation of Uzbekistan's economy. Structural transformation is understood as a long-term process through which economic activity moves from relatively low-productivity activities toward manufacturing, modern services, technology-intensive industries and higher-value export sectors. Foreign investment can contribute to this process by providing capital, introducing advanced technologies, improving management practices, developing human capital and integrating domestic enterprises into international value chains. At the same time, the developmental effect of foreign investment depends on its sectoral composition, domestic linkages, technological content, export orientation and the absorptive capacity of the host economy.

**Keywords:** foreign investment, foreign direct investment, structural transformation, economic diversification, industrial development, technology transfer, export competitiveness, Uzbekistan.

## Introduction

Structural transformation represents one of the fundamental processes of long-term economic development. It involves changes in the composition of production, employment, investment and exports, accompanied by a gradual movement of economic resources toward sectors with higher productivity and greater potential for technological and value-added growth. For developing economies, successful structural transformation is particularly important because dependence on a limited number of sectors or primary commodities can constrain productivity growth and increase exposure to external shocks.

Foreign investment can become an important catalyst for structural transformation. Unlike purely financial capital, productive foreign direct investment can bring together capital, technology, managerial knowledge, international production standards and access to global markets. Foreign enterprises can also stimulate domestic firms through supplier relationships, employee training, competition and knowledge spillovers. However, the presence of foreign capital alone does not guarantee structural transformation. If investment is concentrated in extractive industries, low-value assembly or activities with limited domestic linkages, its contribution to broader economic transformation may remain relatively limited.

For Uzbekistan, the transformation of the economic structure has become increasingly important in the context of industrial modernisation, private-sector development, export diversification and integration into global markets. The country has significant opportunities to attract foreign investment into manufacturing, renewable energy, logistics, information technologies, pharmaceuticals, food processing, textiles, financial services and other sectors with higher value-added potential.

## Literature Review

The theoretical relationship between foreign investment and structural transformation can be explained through several complementary approaches. Dunning's eclectic paradigm emphasises



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ownership, location and internalisation advantages as key determinants of international production [1]. From a host-country perspective, the location component is particularly important because investors tend to select economies where market opportunities, infrastructure, labour resources, institutional conditions and production networks provide favourable conditions for long-term operations.

The contribution of foreign direct investment to economic growth has also been associated with capital accumulation and productivity spillovers. Alfaro et al. argue that the benefits of FDI are influenced by the development of domestic financial markets and the ability of host economies to absorb foreign capital effectively [2]. This indicates that foreign investment should not be considered separately from the broader institutional and financial environment.

Another important dimension is technology transfer. Foreign-invested enterprises can introduce modern machinery, production standards, organisational methods and digital technologies. Domestic firms may benefit through employee mobility, supplier relationships, imitation and cooperation. Nevertheless, these spillovers depend on the technological and organisational capabilities of domestic enterprises. Where local firms lack sufficient skills, financing or infrastructure, foreign-invested projects may operate with relatively weak domestic linkages.

The OECD also emphasises that the quality of FDI matters for sustainable development. Investment can generate different economic, social and environmental effects depending on its sector, business model, employment structure, technological intensity and integration with the domestic economy [3]. Therefore, investment policy should increasingly move from a volume-oriented approach toward a quality-oriented approach.

In the context of Uzbekistan, previous research has highlighted the importance of investment climate, institutional stability, infrastructure and regional attractiveness in determining investment flows [4; 5]. These factors remain relevant, but the structural transformation perspective requires an additional focus on sectoral diversification, domestic value creation, technological upgrading, export sophistication and the development of local production capabilities.

**Research Methodology**

The study applies comparative, systematic, dynamic and institutional approaches to analyse the relationship between foreign investment and structural transformation. The conceptual framework is based on five interconnected dimensions: capital accumulation, sectoral diversification, technological upgrading, domestic linkages and socio-economic outcomes.

The research also applies a transmission-mechanism approach. Under this framework, foreign investment affects structural transformation through several channels:





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The study further considers the role of domestic absorptive capacity. The impact of foreign investment is expected to be stronger where domestic firms, financial institutions, universities, vocational institutions and public agencies possess sufficient capacity to interact with foreign enterprises.

**Results and Discussion**

The analysis demonstrates that foreign investment can influence structural transformation through several mutually reinforcing mechanisms. The first mechanism is capital deepening. Foreign investment enables enterprises to acquire modern machinery, production facilities and technological equipment that may not be fully financed through domestic savings. This is particularly important for capital-intensive industries requiring significant initial investment.

The second mechanism is technological upgrading. Foreign enterprises frequently operate with production technologies and management standards that are more advanced than those available in less-developed domestic firms. When effective channels for knowledge diffusion exist, these technologies can gradually spread through supplier networks, labour mobility, training programmes and business cooperation.

The third mechanism is industrial diversification. Foreign investors can contribute to the emergence of new sectors by introducing production activities that were previously underdeveloped or absent in the domestic economy. This process is especially important for industries with potential for higher value added, such as pharmaceuticals, electrical equipment, machinery, information technologies, advanced food processing and modern business services.

The fourth mechanism is export diversification. Foreign-invested enterprises often possess established connections with international markets and global value chains. Their presence can therefore increase the ability of domestic enterprises to meet international quality, certification and logistics requirements. However, export benefits depend on the extent to which foreign-invested projects generate domestic value rather than simply importing inputs and exporting final products.

The fifth mechanism is human capital development. New investment projects create demand for engineers, technicians, managers, IT specialists and other skilled employees. Training provided by foreign companies can improve the productivity of workers and contribute to the accumulation of knowledge within the domestic labour market.

The sixth mechanism is the development of domestic supplier networks. When foreign enterprises purchase intermediate goods and services from domestic companies, the benefits of investment can spread beyond the foreign-invested enterprise itself. Supplier development can improve quality standards, productivity and competitiveness among local small and medium-sized enterprises.

**Table 1.**

**Main Channels of Foreign Investment Contribution to Structural Transformation**

| Channel | Main mechanism | Expected structural effect |
|---|---|---|
| **Capital formation** | Financing modern production capacity | Expansion of productive capacity |
| **Technology transfer** | Introduction of modern technologies and standards | Productivity and innovation growth |
| **Industrial diversification** | Development of new industries | Reduction of sectoral concentration |
| **Export development** | Integration into international markets | Higher export sophistication |
| **Human capital** | Training and new professional | Improvement of labour |


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| | | |
|---|---|---|
| | requirements | productivity |
| **Supplier development** | Linkages with domestic enterprises | Growth of local value added |
| **Innovation** | R&D and technological cooperation | Development of knowledge-intensive sectors |
| **Infrastructure** | Investment in production and logistics | Reduction of transaction costs |

Source: developed by the author based on the theoretical and institutional literature.

The table demonstrates that foreign investment should be evaluated through a multidimensional framework. The amount of capital attracted is only one component of its economic impact. A project with a relatively moderate investment volume may produce significant structural effects if it introduces new technology, develops domestic suppliers, creates skilled employment and generates exports.

**Conclusion**

Foreign investment can play an important role in accelerating structural transformation of Uzbekistan's economy. Its contribution extends beyond capital accumulation and may include technology transfer, productivity growth, industrial diversification, export development, human capital formation and integration into global value chains.

However, the developmental impact of foreign investment is not automatic. It depends on the sectoral composition of investment, domestic absorptive capacity, quality of institutions, infrastructure, human capital and the strength of linkages between foreign-invested enterprises and domestic firms. Therefore, the effectiveness of investment policy should be assessed not only by the volume of capital attracted but also by the economic transformation generated by that capital.

The proposed approach places investment quality at the centre of structural transformation. Sector-specific investment promotion, technology transfer, domestic supplier development, export orientation, skills formation and transparent monitoring can strengthen the contribution of foreign investment to productivity and economic diversification.

For Uzbekistan, the long-term objective should be to create an investment environment in which foreign capital becomes a catalyst for domestic productive capacity. Such an approach can support the transition from capital-intensive growth toward a more diversified, technology-oriented and value-added economic structure.

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