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Article

Corporate Financing Decisions in Emerging Markets: The Role of Bank Financing, Foreign Investment, and Capital Structure in Uzbekistan

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Abstract: This study examines corporate financing decisions in emerging markets with a specific focus on Uzbekistan, analyzing the roles of bank financing, foreign direct investment (FDI), and capital structure choices during the period 2020–2025. Drawing on capital structure theories (trade-off and pecking-order theories) and empirical data from the Central Bank of Uzbekistan and international sources, the research investigates how firms balance internal funds, bank debt, equity, and foreign capital in a bank-dominated financial system undergoing structural reforms. The findings reveal that bank loans remain the primary external financing source, accounting for the overwhelming majority of corporate debt, while FDI inflows increased significantly (reaching USD 4.4 billion in 2025) and provided an important alternative channel for selected firms. Capital structure decisions are strongly influenced by firm profitability, size, asset tangibility, high interest rates (averaging 22–23.5% on national-currency loans), and the continued dominance of state-owned banks (approximately 63–65% of total banking assets). Equity and bond markets, although expanding, still play a limited role. The study concludes that Uzbekistan's corporate sector largely follows a modified pecking-order pattern adapted to local institutional constraints, and further development of capital markets, reduction of state ownership in banks, and improved investment climate are essential for diversifying financing options and enhancing financial resilience.

Keywords: Corporate Financing, Capital Structure, Bank Financing, Foreign Direct Investment, Emerging Markets, Uzbekistan, Pecking-Order Theory, Financial Sector Reforms

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1. Introduction

Corporate financing decisions play a critical role in determining firm growth, stability, and competitiveness, particularly in emerging markets where financial systems are often bank-dominated, capital markets remain underdeveloped, and institutional frameworks are still evolving. In such environments, the choice between internal funds, bank debt, equity issuance, and foreign investment is shaped not only by classical capital structure theories-such as the trade-off theory and the pecking order theory-but also by country-specific factors, including high interest rates, limited access to long-term finance, state ownership influence, and regulatory constraints [1], [2].

Uzbekistan represents a compelling case study within this context. Since the launch of comprehensive economic reforms in 2017, the country has pursued liberalization of the foreign exchange regime, privatization of state-owned enterprises, modernization of the banking sector, and active attraction of foreign direct investment (FDI). Despite these efforts, the financial system continues to be heavily reliant on commercial banks, while equity markets and alternative financing instruments remain relatively shallow [3]. As a result, corporate capital structures in Uzbekistan are typically characterized by a strong dependence on bank loans, constrained use of equity financing, and growing-but still selective-participation of foreign investors.

This study examines the key determinants of corporate financing decisions in Uzbekistan, focusing on the interplay between bank financing, foreign investment, and capital structure choices [4]. It aims to analyze how firms balance debt and equity in a transitional economy, assess the impact of foreign ownership and FDI on financing patterns, and evaluate the relevance of established capital structure theories in the specific institutional setting of an emerging Central Asian market. By combining theoretical insights with empirical evidence from Uzbekistan, the research contributes to a deeper understanding of corporate finance dynamics in emerging economies undergoing structural transformation [5], [6].

Corporate financing decisions in emerging markets are shaped by the depth of the financial system, the availability of alternative funding sources, institutional quality, and openness to foreign capital. In Uzbekistan, these decisions occur within a bank-dominated financial architecture that has undergone substantial transformation since the 2017 reforms [7]. Between 2020 and 2025, the banking sector expanded rapidly, foreign direct investment (FDI) inflows accelerated, and capital-market instruments began to gain limited traction, yet bank loans remained by far the dominant source of external finance for corporations.

2. Methods and Materials

Classical capital structure theories provide a useful starting point. The Modigliani–Miller propositions assume perfect markets in which capital structure is irrelevant. In practice, the trade-off theory emphasizes the balance between tax advantages of debt and bankruptcy costs, while the pecking-order theory (Myers & Majluf) predicts that firms prefer internal funds, then debt, and equity only as a last resort because of asymmetric information. In emerging markets such as Uzbekistan, high information asymmetry, limited equity-market depth, collateral-based lending practices, and elevated interest rates reinforce pecking-order behavior. Empirical patterns observed in 2020–2025 confirm that profitable firms rely more on retained earnings, larger firms enjoy better access to bank credit, and tangible assets remain the primary form of collateral.

The banking system continued to dominate corporate finance throughout the period. Total assets of commercial banks grew from roughly 400–450 trillion UZS in the early 2020s to approximately 925 trillion UZS by the end of 2025 (an increase of about 20 percent in 2025 alone). The outstanding loan portfolio to the economy expanded to around 600–653 trillion UZS by early 2026, with corporate lending constituting the largest share. State-owned banks retained a dominant position, controlling 63–65 percent of total banking assets and approximately 67–68 percent of the loan portfolio as of late 2025. Non-performing loans (NPLs) rose during the pandemic, reaching peaks near 5 percent in 2021, before declining to 3.5–4.0 percent in 2023–2024 and further to around 3 percent by the end of 2025. Capital adequacy ratios remained comfortable, consistently exceeding 17 percent (well above the 13 percent regulatory minimum).

3. Results and Discussion

Average interest rates on loans in national currency stayed elevated, fluctuating in the 22–23.5 percent range for much of 2023–2025, with corporate loan rates averaging close to 23 percent in 2025. Foreign-currency loans, mainly accessible to exporters, carried lower nominal rates (around 9–10.5 percent) but exposed borrowers to exchange-rate risk [8]. These conditions produced a financing environment in which bank debt remained the primary external source for most firms. Collateral requirements stayed high, preferential lending programs continued to favor certain sectors and state-linked enterprises, and smaller private firms often faced tighter constraints.

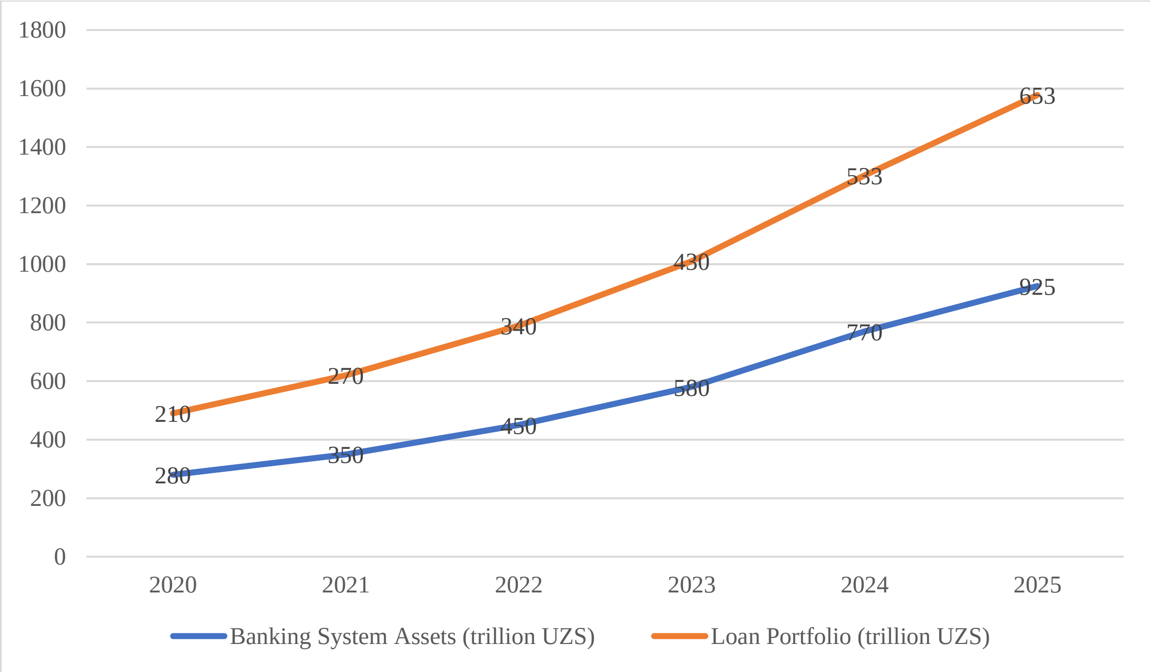

Figure 1. Dynamics of banking system assets and loan portfolio in Uzbekistan, 2020–2025

Source: *Compiled by the author based on data from the Central Bank of the Republic of Uzbekistan (Annual Reports and Statistical Bulletins, 2020–2025) and the Statistics Agency under the President of the Republic of Uzbekistan.*

Figure presents the dynamics of two key indicators of the banking sector in Uzbekistan over the period 2020–2025. The blue line shows the growth of total banking system assets, which increased from approximately 280 trillion UZS in 2020 to 925 trillion UZS by the end of 2025 [9]. The orange line illustrates the expansion of the banking loan portfolio, which rose from about 210 trillion UZS in 2020 to 653 trillion UZS in 2025. Both indicators demonstrate steady and accelerating growth throughout the period, reflecting the rapid expansion of financial intermediation, increased credit supply to the economy, and the overall development of the banking system during the years of economic reforms [10].

FDI inflows provided an important complementary source of capital. Net FDI inflows, which stood at approximately 2.2–2.5 billion USD in the early 2020s, rose to roughly 3.0 billion USD in 2024 and reached 4.4 billion USD in 2025 (about 3 percent of GDP). Cumulative foreign investment and loans attracted since the start of reforms exceeded several tens of billions of dollars.

Foreign ownership influenced capital structure in several ways. Subsidiaries of multinational firms frequently relied more on internal group financing and less on local bank debt. The presence of foreign banks (whose share of system assets remained modest at around 11 percent) contributed to stronger credit-risk practices; some studies indicate lower NPL ratios in foreign-owned banks [11]. At the same time, regulatory limits on non-resident ownership in banking and certain strategic sectors moderated the overall impact of foreign capital on domestic corporate leverage. Although still shallow compared with bank lending, the capital market showed measurable progress. Stock-market capitalization rose from low single-digit billions of USD in the early 2020s to approximately 18.8 billion USD in 2024 and 23.7 billion USD in 2025 (roughly 16 percent of GDP) [12].

Table 1. Key Indicators of Corporate Financing Environment, 2020–2025

Indicator	Approximate Level / Trend (2020–2025)	Implication for Capital Structure
Banking system assets	Grew to ~925 trillion UZS by end-2025 (+20% in 2025)	Expanded capacity for bank lending
State-owned banks' share of assets	63–65%	Continued dominance of relationship-based lending
Loan portfolio to the economy	~600–653 trillion UZS by early 2026	Bank debt remains primary external source
NPL ratio	Peaked ~5% (2021) → declined to ~3% (2025)	Improved asset quality, still cautious lending
Average national-currency loan rates	22–23.5%	High cost of debt discourages excessive leverage
Net FDI inflows	~2.2–2.5 bn USD early period → 4.4 bn USD in 2025	Growing alternative equity / intra-group funding
Stock-market capitalization	Rose to ~23.7 bn USD (2025)	Still limited role of public equity

Source: *Compiled by the author on the basis of data from the Central Bank of the Republic of Uzbekistan, the Statistics Agency under the President of the Republic of Uzbekistan, and the Agency for the Development of the Capital Market (2020–2025).*

The table summarises the main indicators characterising the corporate financing environment in Uzbekistan between 2020 and 2025. It covers the growth of banking system assets, the continued high share of state-owned banks, the expansion of the loan portfolio, the improvement in asset quality (decline in the non-performing loan ratio), persistently high average interest rates on national-currency loans, the increase in net foreign direct investment inflows, and the still limited role of the stock market [13]. The table also highlights the implications of these trends for the capital structure of enterprises, emphasising the continued dominance of bank lending and relationship-based financing, cautious lending behaviour, high cost of debt, and the gradual emergence of alternative equity and intra-group funding sources.

Between 2020 and 2025, Uzbekistan's corporate sector operated in an environment of rapid banking-system expansion, declining but still elevated funding costs, improving asset quality, rising FDI, and gradual capital-market development. Bank financing retained its central role, foreign investment provided selective relief from domestic constraints, and equity markets remained underutilized [14]. These patterns illustrate how classical capital-structure theories adapt to the institutional realities of a reforming emerging market. Further deepening of the capital market, continued reduction of state ownership in banks, and sustained improvement in the investment climate are likely to broaden financing options and gradually shift corporate capital structures toward greater diversification in the coming years [15].

4. Conclusion

Bank financing continues to dominate corporate external finance in Uzbekistan. Between 2020 and 2025, the banking system's assets grew to approximately 925 trillion UZS and the loan portfolio reached about 653 trillion UZS, with state-owned banks retaining a 63–65% share of total assets. This sustained expansion of banking intermediation has reinforced the central role of bank credit in meeting the external financing needs of Uzbek corporations.

Corporate capital structure decisions largely follow a modified pecking-order hierarchy. Internal funds are preferred as the primary source of financing, followed by bank loans (primarily in national currency), then foreign direct investment and strategic equity. Public equity and corporate bonds remain secondary sources and play only a limited role for the majority of firms.

Foreign direct investment has become an increasingly important complementary source of funding. Net FDI inflows rose from around USD 2.3 billion in 2020 to USD 4.4 billion in 2025. This growth has improved access to capital and contributed to the transfer of better governance practices, particularly for firms with foreign participation.

High interest rates (22–23.5% on national-currency loans), elevated collateral requirements, and the still-limited depth of the equity and bond markets constrain more aggressive leverage strategies. These factors reinforce conservative financing behaviour among private firms and limit the overall diversification of corporate capital structures.

Asset quality in the banking sector improved over the period. The non-performing loan ratio declined from pandemic peaks near 5% to approximately 3% by the end of 2025. This improvement has supported a more stable credit supply and reduced systemic risks within the banking system.

Policy implications include the need to accelerate capital market development, continue the privatization and transformation of state-owned banks, strengthen creditor rights, and maintain a favourable investment climate. Such measures are essential to expand the range of financing instruments available to Uzbek corporations and to reduce the systemic dependence on traditional bank lending.

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