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## SCENARIOS OF INVESTMENT AND INNOVATION POLICY IN THE LIGHT OF INSTITUTIONAL TRANSFORMATION

**Abstract:** Subject. The article is devoted to the problems of developing scenarios for the strategy of investment and innovation policy of the state in the conditions of transformation. Goals. Clarification of the definition of the category of investment policy of the state. Development of investment and innovation policy scenarios for the conditions of the Republic of Uzbekistan. Methodology. In the course of the study, such methods of analysis as systematization and generalization were used. Results. Clarifications and the author's interpretation of the economic category "investment policy" are given, trends in the development of the world economy are analyzed, as well as some macroeconomic indicators of the development of the economy of Uzbekistan. Scenarios of investment and innovation policy in relation to the local conditions of the Republic of Uzbekistan are proposed. Conclusions. It is concluded that the objectives of investment policy and innovation strategy are closely interrelated. In conditions of instability of business and investment activity in the world, in order to maintain high rates of economic development of the country, it is necessary to pay more attention to internal growth reserves.

**Key words:** investments, innovations, innovation and investment policy, institutional reforms, strategy, Economy of Uzbekistan.

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### Introduction

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One of the vectors of the country's economic development within the framework of the implementation of the Development Strategy of the new Uzbekistan for 2022-2026 is considered to be high investment activity, which contributes to economic growth and, as a result, is a catalyst for the growth of the welfare of society. This is reflected in the formation of an effective strategy for investment and innovative development of territories. Increasing the volume of investments and improving the efficiency of innovation management are fundamental conditions for the diversification of the national

economy, creating prerequisites for economic growth. The optimal use of investments at both the micro and macro levels depends on the country's production potential and its efficiency.

In conditions of uncertainty, the issues of attracting investments to various sectors of the economy are particularly acute, since the investment process is directly related to economic growth, the increase of which depends on the concentration of domestic investment potential and on the possibilities of attracting foreign investors. Project management is becoming a new developing area of knowledge and practice, which is associated with the identification and assessment of investment risks that affect the decline in investment activity and the effectiveness of economic activities of organizations.

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### Literature review

The discussion of options for developing an investment policy strategy and the resulting options for economic development strategies occupies a significant place in scientific discussions. Thus, the foundations of the theory of economic systems and effective reproduction of social capital were laid in the works of J.K. Galbraith, J.M. Keynes, V.V. Leontiev, D. North, V. Pareto, P. Samuelson, J.Y. Stiglitz, J. Tinbergen, F. Hayek, J. Schumpeter, etc. Issues of strategic management and modeling of investment policy in an innovative economy were dealt with by I. Ansoff, A.A. Vodianov, S.Gulyamov, M.A. Ikramov, A.Y. Malenkov, G. Minsberg, G.A. Parsadanov, I.V. Prangishvili, A.N. Falomyev, L.I. Yakobson, etc.

Having conducted a systematic monitoring of scientific sources<sup>1</sup> in the field of investment policy, we came to the conclusion that the investment policy of the state is a concept of organizing and managing investment activities in the country in order to ensure the achievement of socio-economic development goals. Accordingly, the goals of investment policy depend on what results of the development of socio-economic processes in the country the state wants to achieve.

The main priorities of the investment policy, its content and key points, in turn, proceed from the priorities of the socio-economic policy of the state. At the same time, the need for awareness of the need for spatial balance of policy remains unchanged: investment policy, as well as socio-economic policy, is formed at the expense of the state, but its implementation takes place at the level of territories and industries.

The currently existing developments on the formation of investment policy use a variety of fairly effective research methods, techniques and

approaches. However, the importance of increasing attention to the formation of conditions for an innovative economy in the country, as well as the tightening of competitiveness issues, necessitate the development of investment policy based on new methodological tools.

### Research Methodology

The methodological basis of the research is a process approach. The study takes into account systemic, integration, situational, institutional approaches, which is due to the complexity and multidimensional nature of the scientific problem of developing and implementing an investment strategy. Methods of systems theory, general and strategic management, stakeholder theory, etc. were applied.

The theoretical basis of the study was the scientific provisions contained in the fundamental works of domestic and foreign scientists.

The information and empirical base of the study was made up of international documents of the United Nations, the World Bank, the Interstate Statistical Committee of the CIS, the State Statistics Committee of the Republic of Uzbekistan, as well as factual and empirical materials presented in scientific and practical publications.

### Analysis and results

Currently, the main global problem of the global economy appears to be the development of an adequate strategy for overcoming the financial and economic crisis, which our country is trying to solve using classical monetarist methods — priority attention is paid to regulating the volume of money supply, reducing inflation and supporting financial institutions.

<sup>1</sup> Арсланов, Ш. Д. (2020). Государственная инвестиционная политика региона: проблемы формирования и реализации. *Региональные проблемы преобразования экономики*, (9 (119)), 57-62.

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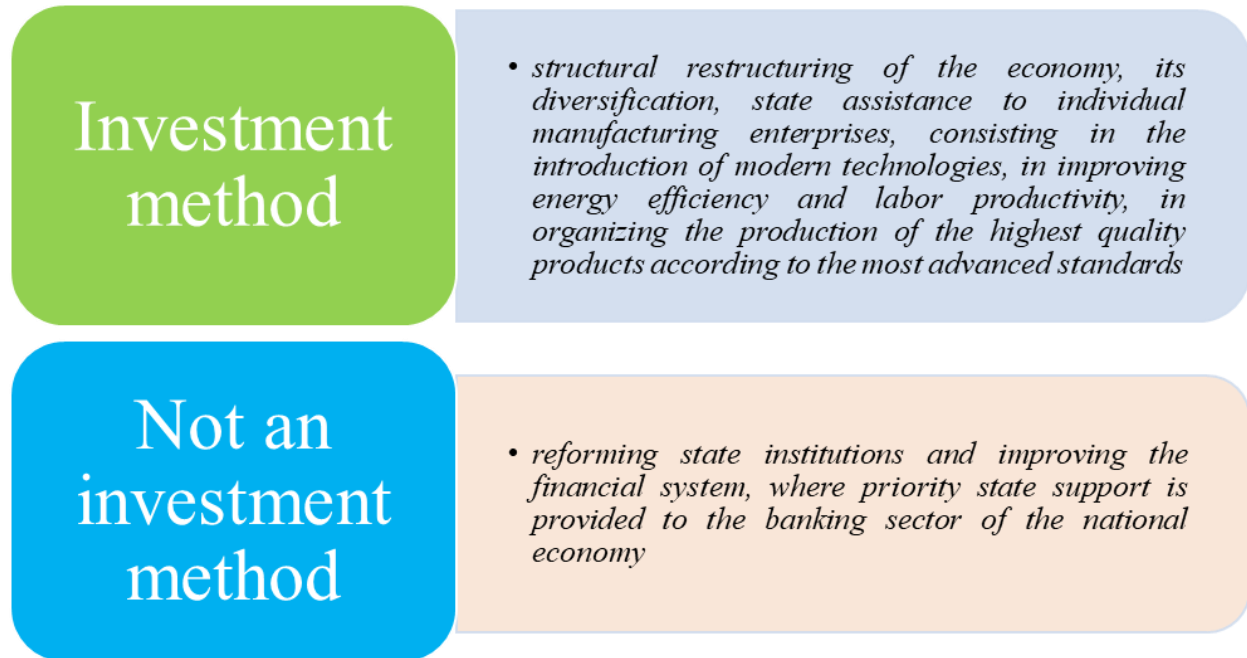
Ferraz, J. C., & Coutinho, L. (2019). Investment policies, development finance and economic transformation: Lessons from BNDES. *Structural Change and Economic Dynamics*, 48, 86-102.

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As world practice shows, the existing ways out of the crisis can be divided into two groups<sup>2</sup>.



**Fig.1. Methods of overcoming the crisis**

As can be seen from the presented figure, the investment method looks quite promising. This is explained by the fact that the investment sphere is the link of the economy, the state of which determines the pace of socio-economic development of the state, the technological level and efficiency of production, competitiveness in global markets and thereby the level and quality of life of the population<sup>3</sup>. Investments in the production of consumer goods and services, the construction of housing and socio-cultural facilities directly affect the living conditions of the population. In this connection, it is difficult to overestimate the relevance of economic growth<sup>4</sup>.

Following this, we can say that with high-quality economic growth, the renewal of fixed production assets takes place, innovative and high-tech activity increases, working conditions at enterprises improve, wages become a form of a decent standard of living for people. This is inextricably linked with the problem of increasing investment activity and improving the investment climate<sup>5</sup>. The growth of

investments and their broad involvement in innovative activities, which adapts the innovations available in world practice and creates new high-tech products, will contribute to the worldwide increase in the competitiveness of the country's economy.

The gradual transition to an innovative economy requires the formation of such a strategy of investment policy of economic growth, which will ensure the transition of the national level of development of production technologies and living standards to a new, higher technical level. It is impossible to make this transition without industrialization and continuous modernization and technical and technological renewal of production.

In our opinion, the country's innovation and investment policy is aimed at improving state regulation, development and stimulation of innovation through investment, structural reforms and improving the standard of living of the population, for sustainable economic development and solving the most

<sup>2</sup> Шпалтаков, В. П. (2018). Проблемы улучшения инвестиционного климата в России. *Вестник Омского университета. Серия «Экономика»*, (1), 56-66.

<sup>3</sup> Власова, О. В. (2019). Инвестиционный кризис как причина стагнации экономики России в условиях санкций. *Вестник НГИЭИ*, (5 (96)), 86-94.

<sup>4</sup> Полонкочева, Ф. Я., Китиева, М. И., & Орцханова, М. А. (2020). Роль государственного регулирования инвестиционных

процессов. *Экономика и бизнес: теория и практика*, (11-2), 198-200.

<sup>5</sup> Цинпаева, Ф. С., & Абдуллаева, З. М. (2019). Современная политика модернизации: институциональные аспекты регионального развития. *Региональные проблемы преобразования экономики*, (9 (107)), 61-66.

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important tasks of the socio-economic system of the state.

From the point of view of the conditions for the formation of an innovative economy, it can be noted that there are a number of problems in the processes of attracting and using investments<sup>6</sup>.

Production in Europe and Central Asia (ECA) is estimated to have grown by 5.8 percent in 2021, indicating a faster than previously estimated recovery in domestic demand for most of this year. The strengthening of economic activity in the euro area and the increase in commodity prices contributed to the growth of exports and the influx of remittances, providing additional support to the recovery processes in the region. The incoming data showed more confident dynamics and contributed to the upward revision of estimates of economic growth rates for 2021 in about 90 percent of the ECA countries.

At the same time, global growth is expected to slow to 4.1 percent in 2022, reflecting the ongoing outbreaks of COVID-19, a reduction in fiscal support and continuing supply bottlenecks. Production and investment in advanced economies are projected to return to pre-pandemic levels next year, but they will remain noticeably lower in emerging market and developing countries (EMDC). Downside risks to the global outlook include a synchronous resumption of the pandemic, further supply disruptions, destabilization of inflation expectations, unexpected financial stress and possible climate disasters<sup>7</sup>. The decision-making bodies of the SFRS countries face problems of increased inflationary pressure and limited budgetary opportunities. In the long term, EMDC countries will need to implement reforms aimed at reducing vulnerability to commodity-related shocks, reducing inequality and increasing crisis preparedness.

By 2023, production in all EMDC regions is expected to remain below pre-pandemic levels, unlike in advanced economies, where the gap is projected to narrow. The region of Europe and Central Asia will be closest to the trajectory that existed before the pandemic, and South Asia will be the furthest from it. Risks that may cause regional forecasts to be revised downwards include ongoing COVID-19 outbreaks, slow progress in vaccination, financial stress, lower-than-expected commodity prices, geopolitical tensions and social unrest, food insecurity, as well as disruptions and damage from extreme weather conditions<sup>8</sup>.

*East Asia and the Pacific region.* According to forecasts, the growth rate in the region will slow down

to 5.1% in 2022, and then in 2023 it will slightly increase to 5.2%.

*Europe and Central Asia.* The growth rate is projected to slow down to 3.0% in 2022 and to 2.9% in 2023.

*Latin America and the Caribbean.* According to forecasts, the growth rate will slow down to 2.6% in 2022, and then slightly increase to 2.7% in 2023.

*Middle East and North Africa.* It is predicted that in 2022 the growth rate will increase to 4.4%, after which it will fall to 3.4% in 2023.

*South Asia.* Growth is projected to increase to 7.6% in 2022, and then slow down to 6.0% in 2023.

*Sub-Saharan Africa.* It is predicted that in 2022 the growth rate will slightly increase, amounting to 3.6%, and will continue to increase in 2023, reaching 3.8%<sup>9</sup>.

Let's consider the situation in relation to the national economy of Uzbekistan.

Competition is still perceived as weak. According to the Bertelsmann Transformation Index, the perception of market competition in Uzbekistan improved from 2016 to 2020, but today it still lags behind a number of other countries in the Europe and Central Asia region, such as Tajikistan, Ukraine, Poland and Russia.

Entrepreneurship remains limited. The density of entry of new firms into the formal private sector — a standard indicator of entrepreneurship - has improved over the past few years, but remains significantly below the regional average and lower than projected per capita income in Uzbekistan.

Formal private firms do not increase in size as they age. The analysis, based on data from the World Bank's enterprise surveys for 2019, shows that formal private firms, especially in manufacturing and services, did not grow as fast as in other large transition economies, such as Vietnam and Russia. In addition, these firms tend to remain small over time: official private Uzbek firms employ an average of 20 employees for up to 10 years, compared with 33.6 employees in similar firms in Vietnam. This gap of 13.6 employees becomes larger (up to 78.6 employees) for firms that are more than 20 years old.

**Reduced labor productivity.** The same micro-level analysis showed that labor productivity (defined as sales revenue per employee) in the formal private sector has been steadily declining over the past decade, with annual growth of -1.2 percent in 2010-2013 and -6.7 percent in 2016-2021. This recent decline indicates poor performance in other areas of entrepreneurship, such as insufficient openness of

<sup>6</sup> Гуляева, Г. Г. (2015). Сущность инновационно-инвестиционной политики. *Современные научные исследования и инновации*, (9-1), 189-192.

<sup>7</sup> Kathuria, S., Yatawara, R. A., & Zhu, X. O. (2021). Spotlight on Outward Foreign Investment and Foreign Direct Investment Policies.

<sup>8</sup> Qiang, C. Z., Liu, Y., & Steenbergen, V. (2021). *An Investment Perspective on Global Value Chains*. World Bank Publications.

<sup>9</sup> <https://www.vsemirnyjbank.org/ru/publication/global-economic-prospects>



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trade, low innovation intensity and weak capabilities of companies.

All this points to a common interpretation: stagnation in the private sector reflects a distorted business environment that does not reward firms with growth potential and prevents the allocation of resources in favor of more efficient firms.

There are many reasons for this. One of the important factors is limited competition in commodity markets, a typical problem for countries with

economies in transition. Indeed, discriminatory interference and regulation continue to make the playing field unequal, especially in markets where State-owned enterprises compete with private firms.

Moreover, there are other reasons such as barriers in the business environment that hinder the development of the private sector, including tax rates, informal sector practices and access to electricity and finance.

### Top 10 Business Environment Constraints: Uzbekistan versus Europe and Central Asia Average

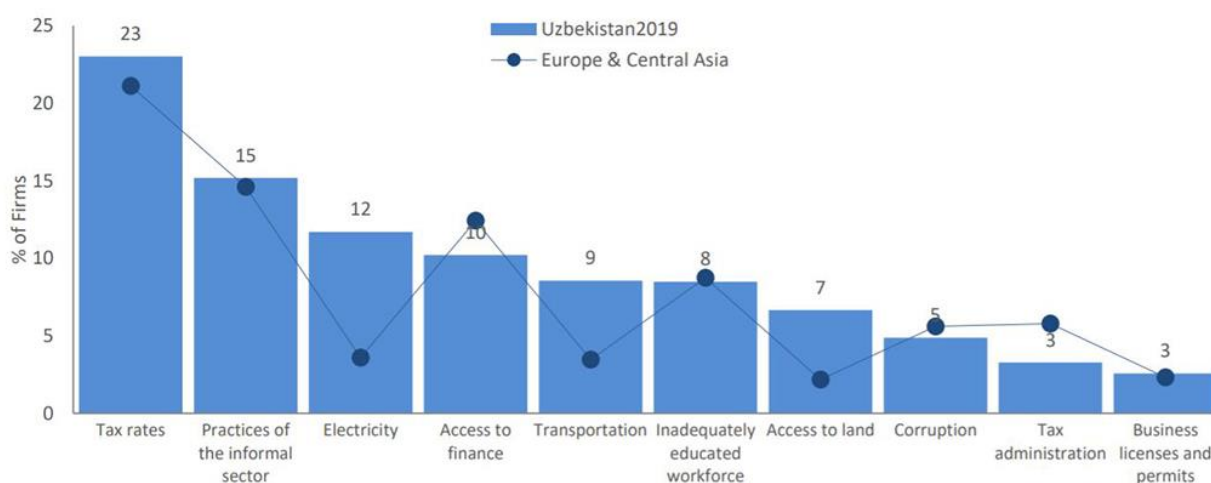


Fig.2. Typical problems of the business sector

These data confirm the need for a comprehensive policy program to optimize the business environment and stimulate the development of the private sector in Uzbekistan. Seven urgent reforms and policies to focus on:

*Active development of competition.* Creating favorable conditions for private firms to compete is just as important as promoting privatization and restructuring of state-owned enterprises. Therefore, it is crucial to continue reducing distorting discriminatory interventions and rules that change the rules of the game, especially in markets where state-owned enterprises compete with private firms. It is necessary to strengthen competitive neutrality, as well as control state aid in order to avoid favoritism and minimize distortion of competition.

*Ensuring that the fiscal system supports the growth of the firm.* The fiscal system should stimulate the growth of companies by balancing tax rates and administrative burden. The fiscal system should raise rates gradually as firms increase in size, so as not to hinder growth, and lower marginal rates to stimulate investment and employment in growing and large companies.

*Mitigation of informal sector practices.* In order to limit the size of the informal sector and redirect

resources in favor of the most efficient firms, public policy should: increase the flexibility of the labor market, reform the social protection system, rationalize the tax system and improve the regulatory framework and the justice system. In addition, there must be conditions for creating good formal jobs so that the informal sector regresses over time.

*Improving access to finance for micro, small and medium-sized enterprises.* This can be achieved by developing competition in the banking sector, reducing state ownership of commercial banks, further reducing targeted government lending, improving bank management and increasing human capital in the banking system. And continuing to strengthen institutions to ensure rapid credit growth and ensure the allocation of financial resources for the most productive projects.

*Promotion of electric power sector reforms.* This is critically important for updating outdated infrastructure and improving the quality and reliability of service. The Government of Uzbekistan is implementing appropriate sectoral reforms to transition to market mechanisms that increase efficiency and update outdated infrastructure. It is also important to ensure effective regulation of competition and pricing.

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*Implementation of an active entrepreneurship support policy.* When implementing the above-mentioned reforms, it is crucial to pursue an active policy aimed at eliminating existing shortcomings that hinder the growth of entrepreneurship. Business support measures should follow two important principles. First, prioritize the growth potential and productivity of firms rather than their survival. Secondly, to combine financial and non-financial tools to strengthen the capabilities of firms so that firms can manage production, learn new opportunities in the market, take on the risk of developing new projects, introduce new technologies and expand activities.

*Addressing skills gaps to ensure private sector growth.* Before the crisis caused by COVID-19, many enterprises reported a lack of skills as a serious deterrent to business development in Uzbekistan. It is estimated that the pandemic has resulted in learning losses equivalent to two years of schooling for children, which affects the potential productivity of the future workforce. Thus, the development of skills in education is an area that requires urgent action.

Uzbekistan faces a difficult task of developing the private sector while abandoning the legacy of a centrally planned economy. Making private firms the backbone of the country's business and economic future is the only sustainable way forward. This will require the coordination of all stakeholders and government agencies, the achievement of a broad consensus and the creation of a reliable framework for monitoring the coordination and implementation of reforms.

Unlocking the full potential of the private sector and entrepreneurship is crucial for Uzbekistan to achieve the 2030 Development Goals and improve the lives of the entire population.

According to World Bank research, investment inflows in Uzbekistan decreased by 26 percent to \$1.7 billion, despite a relatively good macroeconomic situation in which GDP increased by 1.6 percent in 2020, as well as the country's efforts to attract new FDI. The Law on Special Economic Zones (SEZ), adopted in February 2020, for example, promoted new investment projects in the energy sector, as well as in the telecommunications industry. Currently, 22 SEZs are registered and operating in the country. In May 2020, the government announced that 70 companies and consortia from 30 countries had submitted proposals for green energy projects.

In addition, Volkswagen Group (Germany) has launched an investment project in the FEZ from Jizzakh. However, since the country is doubly landlocked, that is, surrounded only by other landlocked countries, border closures and other restrictive measures taken by local authorities and authorities of neighboring countries have affected the economy and delayed investment projects.

Since April 10, 2021, Uzbekistan has been accepted as a beneficiary country under the GSP General Scheme of Preferences.

As a member of the GSP+ system Uzbekistan receives additional economic benefits compared to the standard GSP due to the complete abolition of tariffs on two-thirds of the product lines covered by the GSP, which, in turn, will contribute to export growth and attract additional investment to the country. GSP+'s commitments in the field of sustainable development further strengthen Uzbekistan's position as a reliable and far-sighted economic partner.

The level of use of preferences under the GSP in Uzbekistan currently stands at 87%. The product segments that most benefit from reduced benefits are textiles and clothing, plastic products, as well as fruits, nuts and vegetables, which indicates that Uzbekistan's export structure is already more diverse compared to its neighbors from Central Asia.

The GSP+ scheme offers additional opportunities to increase trade between the EU and Uzbekistan, as tariffs on a number of important export goods, such as fabrics, clothing and plastic products, will be abolished. Despite its relative proximity to the EU market, the trade potential has not yet been fully utilized, since the EU ranks only seventh in the list of export destinations of Uzbekistan.

A comprehensive analysis of the data of the State Statistics Committee of the Republic of Uzbekistan, the Report of The World Bank: Foreign Direct Investment can reveal the following.

Uzbekistan ranks 103rd out of 201 possible in the latest World Bank: Foreign Direct Investment 2019 ranking.

Firstly, the volume of investments per capita remains at a fairly low level - 20% of the world average and ¼ of the average level of the CIS countries.

Secondly, for various reasons, the investment activity of enterprises, the main driver of investment activity, has been declining in recent years - the share of enterprises' funds as a source of investment financing decreased from 32.0% in 2015 to 29.1% in 2021, and the volume of investments at the expense of enterprises increased by only 26.3% compared to 2015.%.

Thirdly, despite the efforts being made, the volume of attracting foreign direct investment (FDI) remains low - 3.6% of GDP by the end of 2018, and 4.1% in 2021, while the optimal level of FDI is 7-10% of GDP, or \$77. At the same time, FDI is one of the key sources of new technologies and experience, and not only a source of additional funds. Their lack is a serious limitation for the successful formation of an innovative economy. At the same time, a significant part of foreign direct investment in fixed capital by the end of 2021 of 61.9 % are in four countries-investors: Russia- 24,2 %, China - 20,4 %, Turkey - 9.2% and Germany to 8.1 %. This indicates a serious

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dependence of foreign capital flows from only 2 countries of the world.

In January-December 2021, 245.0 trillion soums were spent on the development of the economy and social sphere of the Republic of Uzbekistan at the

expense of all sources of financing. sum of investments in fixed assets. In dollar terms, they amounted to \$23.1 billion, and the growth rate by 2020 is fixed at the level of 105.2% (Fig.3).

### Investments in fixed assets by sources of financing

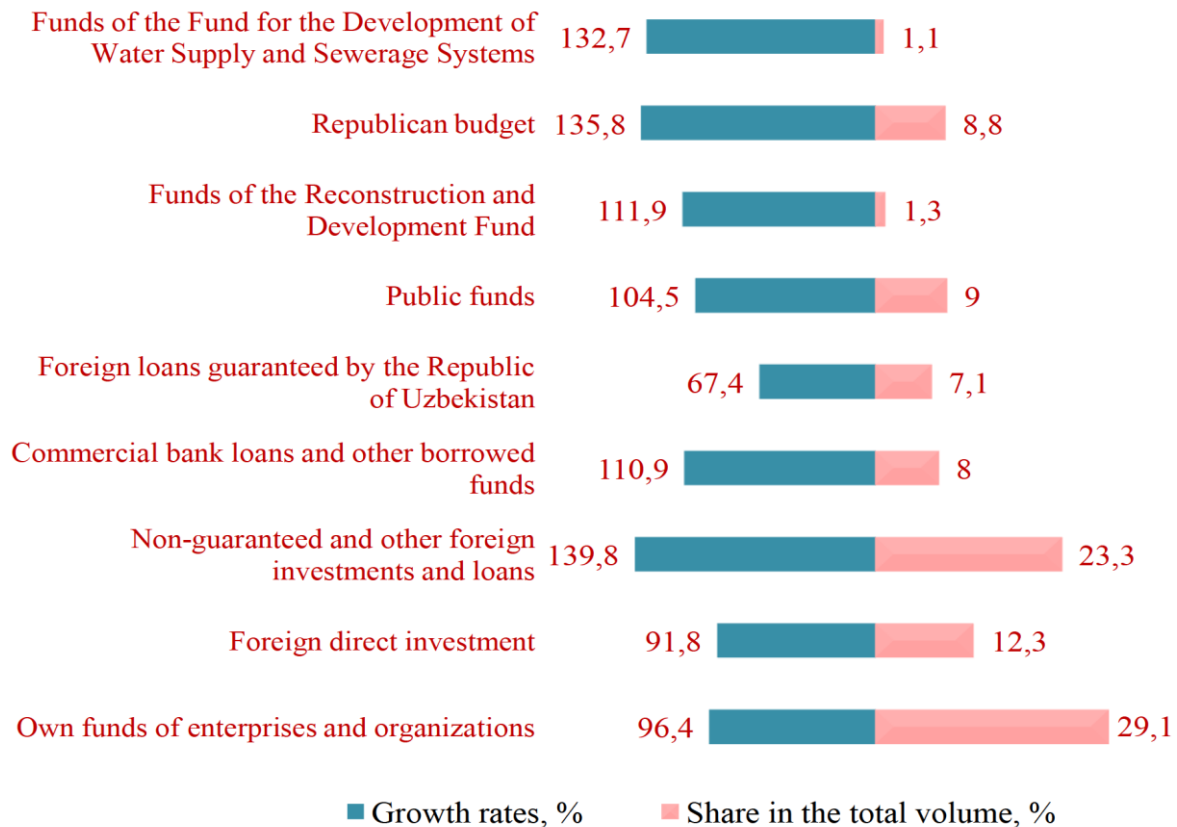


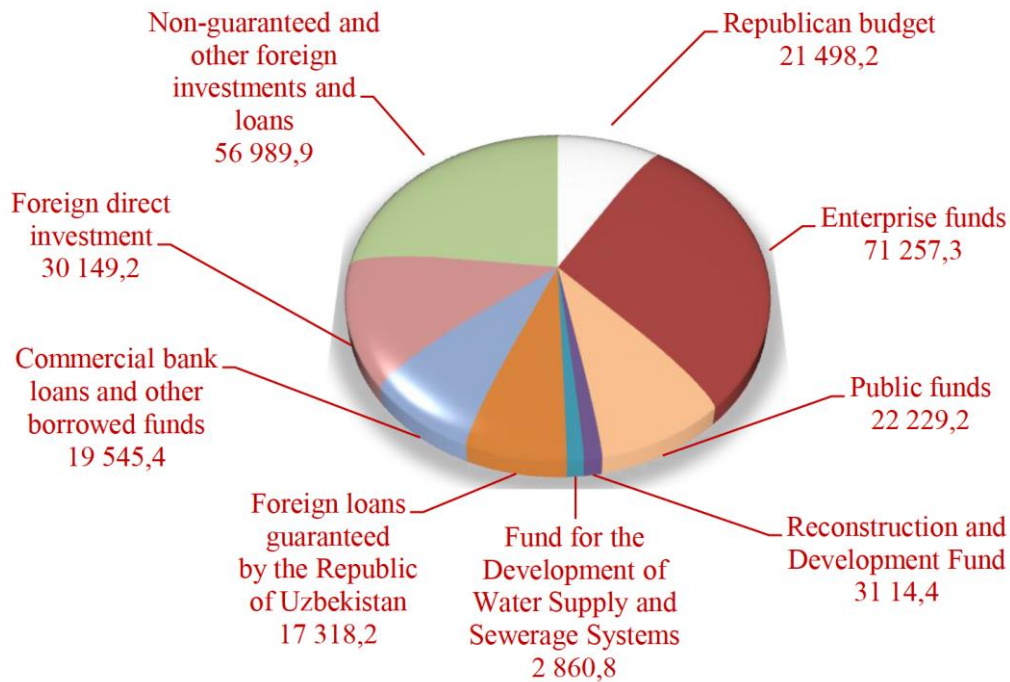
Fig. 3. Investments in fixed assets by sources of financing.

In recent years, measures have been taken to create a large-scale favorable investment climate in the republic, attract and develop foreign investment, in particular foreign direct investment. Thus, as a result of investments made directly at the expense of foreign direct investment, 30,149.2 billion soums were disbursed sum, which, compared with 2020, is 1.8 percentage points less, or 12.3% of their total volume (Fig.3).

The highest indicators and growth rates in terms of sources of financing of investments in fixed assets were noted due to non-guaranteed and other foreign investments and credit funds, which, compared to 2020, increased by 39.8%. 56 989.9 billion. soums of investments in fixed assets was mastered at the expense of non-guaranteed and other foreign investments and loans, and their share amounted to 23.3% and increased by 5.8 percentage points compared to 2020.

<b>Impact Factor:</b>	ISRA (India) = 6.317	SIS (USA) = 0.912	ICV (Poland) = 6.630
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	GIF (Australia) = 0.564	ESJI (KZ) = 8.771	IBI (India) = 4.260
	JIF = 1.500	SJIF (Morocco) = 7.184	OAJI (USA) = 0.350

**Structure of investments in fixed assets by sources of financing, billion soums**



**Fig.4. Structure of investments in fixed assets by sources of financing, billion soums.**

In January-December 2021, the volume of disbursed foreign investments and loans to fixed assets reached 104,457.3 billion. sum (in the dollar equivalent of \$9.8 billion), or 105.2% by 2020 (Figure

5). The share of foreign investments and loans to fixed assets in the total volume of disbursed investments in January-December 2021 was 42.7%.

**Foreign investments and loans to fixed assets, billion soums**

	<i>Total</i>	<i>including:</i>		
		<i>foreign direct investment</i>	<i>foreign loans guaranteed by the Rep. of Uzb.</i>	<i>other foreign investments and loans</i>
<b>Republic of Uzbekistan</b>	<b>104 457,3</b>	<b>30 149,2</b>	<b>17 318,2</b>	<b>56 989,9</b>

**Fig.5. Foreign investments and loans to fixed assets, billion soums.**

In the total structure of foreign investments and loans, foreign investments reached 39 879.4 billion. sum and, respectively, 64 577.9 billion. sums are accounted for by foreign loans.

Fourth, the main volume of investments is directed to the development of the manufacturing

industry. The industry has mastered a significant amount of foreign investments and loans, which amounted to 39,213.1 billion. sum, or 37.5% of their total volume.



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At the same time, about 6% is directed to more important industries from the point of view of the formation of an innovative economy -electrical engineering and mechanical engineering, as well as science and education. A similar situation is observed in the structure of the distribution of foreign investments.

As for the actual investment in innovation, the total amount of costs for all types of innovations (technological, marketing and organizational) has decreased approximately, and their dynamics are volatile.

There is still an imbalance in the structure of costs by type of innovation - technological innovations occupy the largest share (74.8% in 2018), almost equally process and product. The prevalence of costs for technological innovations, without the development of marketing and organizational ones, although it contributes to the growth of enterprises in the short and medium term.

Based on these problems, taking into account the set goal of the investment policy, three scenarios of the strategy can be considered:

I. the script. Identification of priority sectors of the economy and worldwide state support for their development. The basis for choosing priority industries can be an analysis of available resources and the potential for the development of industries, identifying gaps in the value chain and directing investments to "close" the gap in the chains.

At the same time, 2 stages can be distinguished here:

- the first 5-10 years - creation of national value chains and national brands;
- the next 10-15 years - the integration of Uzbek enterprises into international value chains.

II. scenario. Development based on the theory of the stages of development of the economy of the World Economic Forum - from the resource economy to the economy based on the growth of productivity of factors of production and further to the economy based on innovation.

III. the script. Active formation of clusters in strategic areas of the economy and, accordingly, the direction of investments to stimulate and develop this process. In some respects, this approach echoes the first two. However, unlike the first option, it is proposed to focus not on a single industry, but on their complex. Accordingly, unlike the second option, it is supposed to focus on investing in personnel training

and infrastructure not in the economy as a whole, but within a separate set of industries.

Each of these strategy scenarios is acceptable from the point of view of achieving the ultimate goal - the formation of an innovative economy. However, the most relevant is still the combination of the considered scenarios, depending on the characteristics of industries and regions, as well as the current situation.

### Conclusion/Recommendations

The development of investment institutions, strengthening the market infrastructure, increasing the level of financial literacy of the population, ensuring the transparency of the activities of joint-stock companies, strengthening the protection of shareholders' rights will ensure an increase in the participation of foreign capital and the population in the stock trading market of domestic enterprises.

In general, summarizing the above, it can be noted that the strategy of economic development, first of all, investment potential, for the long term, is necessary in order to purposefully regulate the investment field and flows.

The priority direction of the investment policy is to increase the volume of foreign direct investment inflows. The instability of the regulatory environment and the lack of transparency of business conditions, the continuing problems with the stability and development of infrastructure, the protection of the rights of investors and owners significantly limit the inflow of foreign direct investment in these conditions, along with the solution of these problems, there will be the introduction of mechanisms for the targeted attraction of foreign capital through special incentive measures, the establishment of cooperation between the business circles of the republic and foreign countries, as well as attracting foreign investors to acquire state assets, including in the banking sector.

In conditions of instability of business and investment activity in the world, in order to maintain high rates of economic development of the country, it is necessary to pay more attention to internal growth reserves. The emphasis on the expansion of domestic demand, a comprehensive increase in the level of savings by accumulating free funds of the state, enterprises, and the population for investment purposes will keep the process of expanded reproduction at a sufficiently high level.

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