
CENTRAL ASIA: A LAST CHANCE FOR CHANGE

I. OVERVIEW

The Annual Meeting of the European Bank for Reconstruction and Development (EBRD) commencing on 3 May 2003 is an opportunity to assess frankly and honestly the records of the governments of Kazakhstan, Kyrgyzstan, Tajikistan, Turkmenistan and Uzbekistan. If the chance is grasped to push for reform in a more coordinated and concerted way, the controversial decision to hold this meeting in Tashkent will prove well justified. If it is not, and any impression is left that the location of the meeting is a mark of approval for Uzbekistan's current policies, there is a major risk of further deterioration in both the economic and security climate in Central Asia.

Uzbekistan was certainly a difficult choice for the annual meeting of a major international financial organisation committed to democratic principles and open economies.¹ According to the Heritage Foundation and the *Wall Street Journal*, it ranks 149th out of 156 countries in terms of economic freedom, worse than Burma, although slightly better than Cuba. In Freedom House's rankings of political freedoms and civil rights, it is termed "not free", with a ranking of 6.5 out of 7 (Saddam Hussein's Iraq scored 7, as did Turkmenistan).

Instead of enjoying the transition to democracy and open economies as experienced in much of Central Europe, in Uzbekistan as elsewhere in Central Asia a different type of political and economic system has

begun to emerge, closer to authoritarian feudalism than democracy. Economies have remained largely closed to free competition and frequently distorted by government intervention and corruption.

The reality of these systems is seldom recognised by the international community, which has too often taken government rhetoric about democratisation and reform at face value. The problem is not just a lack of political will to pursue reforms, but in many cases active political actions in opposition to reform, while retaining a façade of pro-Western rhetoric to maintain the flow of credits and grants.

Central Asian states can sometimes appear to be relatively stable on the surface, but this stability is a dangerously thin veneer over a host of unresolved tensions. The issue at stake is not merely the economic prosperity of Central Asia, but its political stability and the potential for future unrest that would have a huge impact on the wider region.

All the states of the region face tremendous challenges:

- ❑ poorly performing economies that have failed to lift living standards since the end of the Soviet Union;
- ❑ heavy reliance on one or two export commodities for economic survival, increasing the risk of economic shocks, corruption and civil conflict;²
- ❑ unrepresentative and rigid political structures, with limited mechanisms for the transfer of power;

¹ Unlike most international financial institutions, the EBRD has a specifically political agenda: "to foster the transition towards open market-oriented economies and to promote private and entrepreneurial initiative in ... countries committed to and applying the principles of multiparty democracy, pluralism and market economics." Charter of the European Bank for Reconstruction and Development, available at www.ebrd.org. See also on the same site, "Political Aspects of the Mandate of the European Bank for Reconstruction and Development".

² Paul Collier, "The Market for Civil War", *Foreign Policy* May/June 2003. Collier, the head of the World Bank Development Research Group, argues that countries with poor and declining economies, a reliance on natural resources and a failure to enact real economic reforms are most at risk of conflict. He suggests that the chances increase when the countries have already suffered civil conflict or high levels of violence – or are mountainous.

- ❑ failure to develop working regional cooperation on a range of key issues, from border management and security to trade and water distribution;
- ❑ vulnerability to the growth of extremist political and religious groups;
- ❑ organised crime, particularly linked to narcotics transit from Afghanistan;
- ❑ young and rapidly growing populations with limited prospects for education, work and health; and
- ❑ a complex international environment, with major states competing for influence in the region.

Now is a good time to reassess the problems and prospects of Central Asia. The EBRD meeting offers just such a chance but it needs to take a realistic view of the real problems that the five states face and offer practical solutions that will make a difference.

The EBRD has set out some broad themes for discussion at the meeting, addressing:

- ❑ political will as a vital element in improving the investment climate;
- ❑ responsible business and the impact of foreign investment on ordinary people;
- ❑ obstacles to trade and regional cooperation;
- ❑ water disputes among Central Asian states; and
- ❑ nurturing small business as an engine of economic growth.³

This briefing provides an overview of the issues and suggests some ways in which the pressure for change from organisations such as the EBRD could turn into real reform.

II. CENTRAL ASIA: BACKGROUND

The Central Asian republics faced difficulties on independence in 1991 that can scarcely be overstated. States had to be created and government institutions developed almost from scratch, and long-dormant international links revived, all while keeping

potential ethnic, social and political conflicts under control.

Some leaders continue to insist that the time has been too short to develop democratic systems or bring prosperity to their peoples. But the differences now emerging among the Central Asian states clearly show that some have managed better than others to move towards open societies and prosperous economies. The varied success experienced across the region since independence is partly the result of economic factors influencing development, but much more of specific policy decisions, and political and economic choices made by leaders.

A. KAZAKHSTAN

For most Uzbeks, Tajiks or other Central Asians, Kazakhstan looks like a success story. Indeed, its economic performance has improved markedly in recent years, and living standards are rising. However, the outward economic success visible in the lively city of Almaty can be deceptive. Although President Nursultan Nazarbayev can claim credit for economic progress and keeping a very diverse country together, his authoritarianism and the huge corruption at the top of the political system threaten to undermine these very real achievements.

In 2001 many younger officials and business-people, increasingly frustrated by Nazarbayev's authoritarian policies, attempted to create a powerful opposition movement. They founded the Democratic Choice of Kazakhstan (DCK) in November of that year, and the movement quickly gained support. But under growing political pressure, and facing a corruption scandal involving secret Swiss bank accounts, Nazarbayev responded with a severe crackdown on both the media and the DCK.

Mukhtar Ablyazov and Galimzhan Zhakiyanov, two DCK leaders, were arrested and jailed, as was the journalist Sergei Duvanov, the latter on a dubious rape charge.⁴ Though weakened and divided, the opposition has not gone away, and allegations of corruption continue to dog the president. In his annual state of the nation address in early April 2003, Nazarbayev promised wide-ranging liberalisation,

³ See the program of the Annual Meeting, at www.ebd.org/am.

⁴ See "Prominent Opposition Journalist Convicted in Kazakhstan on Rape Charges", www.eurasianet.org, 28 January 2003; European Parliament Resolution on Kazakhstan, 13 February 2002, at www.europarl.eu.int.

but until dissidents are released, there will rightly be scepticism that this is more than a rhetorical ploy.

B. KYRGYZSTAN

President Askar Akayev has managed to achieve the most liberal political and economic atmosphere in the region, but fine words do not always translate into good practice. High-level corruption and poor governance have inhibited economic growth; journalists and independent media are under serious pressure; and Akayev's main political opponent, Feliks Kulov, remains in jail on what seem to be politically-motivated charges.

Kyrgyzstan, with its lack of resources and formidable geography, was always going to face difficulties building a viable economy. It is hugely dependent on the output of a single gold-mine.⁵ Some economic reforms have been made, but much more could be achieved if a serious effort was undertaken to tackle corruption at all levels and if the presidential family and friends restricted their appetites to control the most lucrative sectors.

This increasingly closed political system reached a crisis in March 2002, when police shot dead five protestors in the southern district of Aksy. The resulting anger with the government led to months of protests and marches. Weaknesses in the opposition and some apparent concessions from the government produced an easing of tensions but dissatisfaction with the government remains high, particularly in the South.⁶ A referendum was held on 2 February 2003 that approved Akayev's term of office until 2005 and amended the constitution. But there is little doubt that the results were widely falsified,⁷ and that most of the population remains unconvinced by the leadership's rhetoric.

⁵ Real GDP, excluding gold and energy, recorded modest growth in 2002 of 3.5 per cent, according to the IMF. But a collapse in production at the mine, caused by a landslide, ensured that overall GDP contracted by 0.5 per cent.

⁶ See ICG Asia Report N°37, *Kyrgyzstan's Political Crisis: An Exit Strategy*, 20 August 2002.

⁷ The opposition claimed that turnout was below the required 50 per cent. See "Opposition details violations during Kyrgyz referendum", *Kyrgyzstan Daily Digest*, 7 February 2003, www.eurasianet.org; and International Helsinki Committee, "Letter to the President of the Kyrgyz Republic", 7 February 2003.

C. TAJIKISTAN

Tajikistan experienced a brutal civil war from 1992 to 1997, ending with a compromise settlement that included the opposition Islamic Renaissance Party (IRP) and others in a coalition government. However, since 1997 the government has increased pressure on the opposition and become steadily more centralised around a small decision-making circle close to President Imomali Rakhmonov.

The government has made great strides in improving the security situation in the country, but it has been unable to open up the economy sufficiently to produce a real rise in living standards for much of the population, 80 per cent of which survives below the poverty line. There is huge need for more investment and growth that affects people's daily lives.⁸

At present the most attractive option for many is to work abroad. At least 500,000 Tajiks work at casual jobs in Russia, often under dangerous conditions and with no legal protection.⁹ The remittances migrants send home may amount to as much as U.S.\$600 million per year.¹⁰ The economy's other major crutch is international aid, which amounted to at least U.S.\$230 million in

⁸ GDP growth in Tajikistan of 9 per cent in 2002 seems like a sign of healthy progress, and it does reflect some recovery from the lows of the civil war period. However, GDP figures are a poor indicator of economic performance in such states. Statistics are not always reliable, and formal statistics tend to relate mainly to a small formal economic sector dominated by resource exports. Capital flight ensures that improved incomes in these sectors has limited impact on the wider population. Real changes in the economy that affect the majority of the population are much more difficult to calculate but almost certainly would present a less attractive picture. Similar caveats need to be applied to other growth figures in the region. See Appendix A for full figures.

⁹ There are no confirmed figures: unofficial estimates claim that up to 1.5 million Tajiks work abroad at one time or another. Reports suggest that at least 500,000 to 700,000 Uzbeks have left their homeland in search of work. *Hurriyat* [Tashkent], 9 April 2003, p. 3. The issue of migration is becoming critical for Central Asia, not only to Russia and further afield, but also within the region. Uzbeks and Tajiks now travel to Kazakhstan and even Kyrgyzstan in search of work. Most migration is informal or illegal, leaving migrants vulnerable to abuse or deception. Migration also easily leads into human trafficking.

¹⁰ There are no reliable figures since most remittances are not transferred through banks. See ICG Asia Report N°51, *Tajikistan: A Roadmap for Development*, 24 April 2003.

2002.¹¹ Dependence on remittances and external aid leaves the country dangerously vulnerable to external pressures. There is little concept of how to move economic development forward, and on present trends, Tajikistan will face serious long-term problems, as health and education worsen dramatically, and increasing numbers of people join the exodus abroad.

D. TURKMENISTAN

The worst situation in the region is in Turkmenistan. President Saparmuryat Niyazov has succeeded in almost destroying the society he leads. Every day he stays in power represents a further decline in hope that Turkmenistan will ever emerge as a prosperous and pluralistic society. He survived an apparent assassination attempt in late 2002, but this led to a further crack-down on anyone regarded as potential opposition to his regime. Major gas and oil deposits give the country great economic potential. In the past two years it has posted double-digit growth, as gas exports have increased. But most of this money ends in a presidential fund, used mainly for grandiose construction projects. Little trickles down to the population.¹²

Niyazov – or Turkmenbashi (Father of the Turkmens) the Great – as he has named himself, has developed a cult of personality exceeding that of Iraq's former leader Saddam Hussein. His sayings and thoughts, collected in a pseudo-spiritual guide, the *Rukhnama*, forms the main textbook for schoolchildren and students. Statues and portraits of the leader are everywhere; even on television there is no escape: his profile rotates in the corner of the screen.

Major gas deals with Russia and Ukraine ensure a continued source of funds for this dictatorship. But rising public and elite discontent threatens long-term

political stability. While Niyazov remains in power, society continues to decline, with education seriously damaged and a new generation emerging that has little hope for the future and increasingly seeks escape through migration, drug abuse or crime.

E. UZBEKISTAN

President Islam Karimov's repressive policies have been justified by the government as a response to the threat of Islamist radical forces. But much of this repression seems only to have radicalised political opposition.¹³ There have been no free elections during the past decade, and the repressive apparatus of the interior ministry has become ubiquitous. The security forces are responsible for systematic human rights infringements, not just against political opponents or religious activists, but also against business-people and traders.¹⁴

Uzbekistan has rejected the market reforms of Russia and Kazakhstan to follow its own model of economic development, a damaging mixture of state interference, import-substitution policies and widespread corruption. The economy survives only on exports of gold and cotton, and the population is increasingly frustrated and impoverished. Serious reforms are necessary to stave off social discontent or worse.

An IMF program in 2002 offered assistance if a staff monitored program designed to lead towards convertibility of the Uzbek currency was fulfilled. Not only did Uzbekistan fail to achieve the IMF's benchmarks, it also instituted extensive tariffs and regulatory restrictions on import-export activity that temporarily emptied bazaars across the country and left many small business-people unemployed or drawn into criminal contraband networks.¹⁵

The way forward for Uzbekistan is not easy. Its political elite is engaged in an increasingly active

¹¹ ICG interview, Emin Sanginov, Director of the Aid Coordination Unit under the Executive Administration of the President of the Republic of Tajikistan, Dushanbe, 3 December 2002.

¹² See ICG Asia Report N°44, *Cracks in the Marble: Turkmenistan's Failing Dictatorship*, 17 January 2003. Turkmenistan's dependence on gas exports also demonstrates the limited utility of its growth figures. GDP fell by 25 per cent in 1997, when gas exports were suspended in a payment dispute with Russia; GDP rose by 16 to 20 per cent per year as gas exports were resumed. The majority of the population remained consistently poor regardless of the rates.

¹³ As one resident of the remote region of Surkhandarya put it: "We never had anything to do with politics or religion, but now I feel like fighting the government myself. If I had to choose between this government and the IMU [Islamic Movement of Uzbekistan – Islamist radical movement] I would choose the IMU". ICG interview, Surkhandarya, 2003.

¹⁴ The UN Special Rapporteur on Torture, who visited Uzbekistan in November-December 2002, considered torture to be "systemic" in the justice system.

¹⁵ See ICG Asia Report N°46, *Uzbekistan's Reform Program, Illusion or Reality?*, 18 February 2003.

struggle around the presidential succession, and there is little impetus for further reforms. Without significant liberalisation, however, the economy is destined to decline further, and with it the political stability that the government has prized above all.

III. POLITICAL WILL AND THE INVESTMENT CLIMATE

The mixed record on political and economic progress in the region is reflected in diverse success at attracting foreign investment. In all the countries, with the partial exception of Kazakhstan, foreign investment has hit rock bottom. By the end of 2000, Tajikistan had gained just U.S.\$30 per capita in cumulative foreign direct investment in the decade since independence. In Uzbekistan the figure was U.S.\$37. Only Kazakhstan, with U.S.\$564 per head, has a respectable record over the past decade. To put these numbers in perspective, Croatia attracted about U.S.\$214 per capita in 2002 alone, while Uzbekistan received just U.S.\$2.5 per capita in the same year.¹⁶

This failure to attract inward investment has only partly to do with economic potential or resources. The real problems for investors are political systems that are too close to business and riddled with corruption, economic rules that are designed to favour the status quo, and rulers who have little interest in opening up the economy for fear of losing political dominance. The idea that authoritarian rulers can somehow push through unpopular reforms may have some backing in political science literature but there is little evidence for it in Central Asia. President Karimov's annual promise since 1999 that Uzbekistan will achieve a convertible currency remains unfulfilled not least because authoritarian rule has permitted the capture of policy-making by vested interests that benefit from the status quo.

This negative influence on policy-making of powerful vested interests that would lose from reforms is evident in all five countries. Their predominance in

policy-making processes has been a major block to both economic reform and democratisation. It has led to the development of political systems that to a greater or lesser extent rely on coercion or feudal types of resource distribution and denial to maintain themselves. These authoritarian-feudal systems of power, though some are much more liberal than others, all share three key features:

- ❑ government and big business are almost inseparable, with officials relying largely on rent-seeking and resource exports for profit;
- ❑ the private sector is weak, unable to organise, highly dependent on state authorities, and limited in its ability to grow into an independent force; and
- ❑ the mass of the population is involved in subsistence activities, unemployed, or migrating to other countries to find work.

Such systems provide some short-term political stability, since they either co-opt or sideline potential opposition and retain control over elites through feudal allocations of resources. But they also ensure long-term economic decline and a growing crisis of legitimacy for elites, as patrimonial policies such as welfare and subsidy programs can no longer keep up with population growth and aspirations. Thus the present political systems, in which elements opposed to reform occupy powerful positions, represent not just a block on economic growth and inward investment, but also a potential source of future instability.

A. POLITICAL ELITES AND CHANGE

Many of the key political issues faced by the Central Asian states are linked to elite politics. The leadership that came to power in the early 1990s emerged largely from Soviet-era elites. In Kazakhstan, Uzbekistan, and Turkmenistan, former first secretaries of ruling Communist Parties swiftly rearranged the labels and emerged as rhetorical champions of independence, democracy and market economics.

After twelve years of independence there has been no real transfer of power in any of the Central Asian states. President Karimov has been in office since 1989, and after a dubious referendum in 2002, had an extra two years added to his term, now slated to end in 2007. President Akayev of Kyrgyzstan has been in control since 1990, although he has promised to step

¹⁶ Figures from Economist Intelligence Unit. According to EBRD estimates, Uzbekistan attracted just U.S.\$65 million in foreign direct investment in 2002. However, Deputy Prime Minister Elyor Ganiev claimed that foreign investments in 2002 totalled U.S.\$650 million and that overall foreign investments since independence totalled U.S.\$14 billion. "Foreign investments in Uzbekistan total \$650 in 2002", 7 April 2002, available on the National Bank for Foreign Economy Activity's website, at <http://eng.nbu.news>.

down in 2005. In Turkmenistan, President Niyazov has been at the top since 1985.¹⁷ He shows no signs of relinquishing power in the near future, having been declared president for life in 1999. President Rakhmonov of Tajikistan came to power in 1992 in the midst of civil war and is holding a referendum in June that would theoretically allow him to rule for two further terms of seven years after elections due to be held in 2006.¹⁸ Finally, in Kazakhstan, President Nazarbayev is going on fourteen years as leader, and he, too, shows no sign of giving way to an increasingly impatient younger generation.

The period when these leaders came to office was very different from today. New challenges require a new generation of leaders to face them. The ability of the present leaderships to arrange a peaceful transfer of power and the political complexion of this new generation will be the main determinants of how Central Asia faces the risks and opportunities of a new global order.

There is a huge gap between generations in Central Asia in their world views, their education and their understanding of political and economic realities. It would be a mistake to believe that new leaders would necessarily be more pro-Western, or somehow instinctively wedded to Western ideas of political democracy or market economics. Indeed, disappointment with the West is widespread among the younger generation in Central Asia, not least because the apparently huge investments made by Western institutions seem to have had so little impact on most lives.

The lack of workable political succession mechanisms in the Central Asian states leads to long-term uncertainty for investors. There is no guarantee that new leaders will respect contractual obligations, and in several cases, there is a high likelihood that succession will be accompanied by instability and even violence. Managing this change and promoting new reform-minded elites will be major challenges over the next few years. Peaceful successions would be made easier by increased possibilities for wider political participation sooner rather than later. Opening up political systems would

also begin to break the stranglehold that small elites hold on the economy.

B. RULE OF LAW AND HUMAN RIGHTS

If democracy is not embedded in any of these states, rule of law and respect for human rights are equally absent. Again the situation differs among the five states, although in each the legal system is highly dependent on the regime and cannot be considered independent. In each, state security forces are used as political tools against the opposition and, at least in Uzbekistan and to a certain extent Turkmenistan, have become significant political players in their own right.

There is unlikely to be serious economic development without much more attention to the justice sector. Without an independent judiciary business people have no recourse in commercial disputes beyond approaches to authoritative informal leaders. The security forces interfere constantly in business operations and often have their own profitable, semi-legal sidelines, through either protection of certain businesses or direct involvement in commercial operations.¹⁹

Human rights abuses are widespread, and there has been little recent improvement despite increased international attention since 11 September 2001. The situation is worst in Turkmenistan where the apparent assassination attempt on President Niyazov was followed by a crack-down on a wide range of officials and their relatives, most of whom were imprisoned without any real trial.²⁰ In Uzbekistan there were some signs of improvement in 2002, with the registration of two human rights groups and a decrease in arrests of religious activists. But the reality remains depressing, with a highly repressive state continuing to command loyalty largely through fear. This widespread fear is noticeable at all levels, from officials afraid to take policy initiatives or make public statements, to entrepreneurs reluctant to begin or expand their business because they expect only problems from the authorities. It is the very opposite of an environment in which risk-taking entrepreneurs are likely to thrive.

¹⁷ Niyazov became Chairman of the Council of Ministers in 1985, then First Secretary of the Turkmen Communist Party, and in 1990 became Chairman of the Supreme Soviet. In June 1992 he was elected president with 99.5 per cent of the vote.

¹⁸ President Rakhmonov became Chairman of the Supreme Soviet in 1992; he was first elected president in 1994.

¹⁹ See ICG Asia Report N°42, *Central Asia: The Politics of Police Reform*, 10 December 2002.

²⁰ See ICG Report, *Cracks in the Marble*, op. cit.

Human rights abuses do not only affect religious activists or political opposition. The use of torture and beatings by police makes citizens extremely fearful of dealing with law enforcement officers, even when they have legitimate complaints. The result is that businesses rarely resort to legal action when they are victims of intimidation or corruption, especially if the offending party is the police themselves. Better to pay a bribe or sell out entirely, many reason, than risk becoming entangled with the police. Human rights abuses and an unreformed justice system thus present serious obstacles to the development of a functioning, law-based economy.

C. CORRUPTION AND PUBLIC ADMINISTRATION

Fighting corruption has been at the forefront of international development rhetoric for a decade or more, and valuable lessons have been learned around the world about what works and what doesn't. Little of this experience has been brought to bear by international organisations in Central Asia, which as a region ranks as one of the world's worst on most governance indices.²¹ Transparency International's Corruption Perceptions Index puts Uzbekistan and Kazakhstan in 68th and 88th place, respectively, out of 102 countries.²²

Corruption starts at the very top in each country. Kazakhstan remains the leader in sheer volume, partly because there is simply more to steal. When it was revealed that President Nazarbayev had deposited U.S.\$1 billion of state finances under his own name in a Swiss bank account, he seemed surprised by the extent of criticism. From his perspective he had done nothing wrong; as "Father of the Nation", there was little psychological difference between state and presidential finances. Indeed, Prime Minister Imangali Tasmagambetov defended Nazarbayev's actions by saying that the account had twice helped the government avert financial crises.²³

The same psychology of minimal differentiation between state and personal finances is present throughout Central Asia. Corruption at the top of government ministries and agencies ensures that malpractice spreads down through the system. There is a widespread practice of government officials gaining posts not through merit but through connections or simply by purchase. This happens at almost all levels. As one Kyrgyz police officer complained to ICG: "I went on a business trip for two weeks, and when I came back somebody else had already bought my job for U.S.\$3,000".²⁴

This practice has an obvious impact on the effectiveness of government organs. The governor or tax inspector who has paid a large sum to receive his appointment needs to recoup his investment as fast as possible. Since most officials are not elected, they can be removed as quickly as they were appointed. So for many officials, it is a nervous race against time to get back the money they have paid before a further round of reshuffles moves them on to another post. In 1993-2002 the average tenure for a hokim (regional governor) in Uzbekistan was less than three years.²⁵

Corruption has the potential to undermine state structures fundamentally and leave criminal groups or local "authorities" in effective control of parts of the economy or particular territories. Kyrgyzstan has made big efforts to create structures to attract investment, with a Secretariat on Foreign Investments, a Consultative Council on Foreign Investments; and a "one-stop shop" for investors, where, theoretically, they can solve all bureaucratic problems under one roof. But the reality is somewhat different.

In the remote region of Aravan, to the south of Osh, a successful cotton factory run by a Russian investor was seized in December 2002 by a conglomeration of shady businessmen from across the border in Uzbekistan. The owner was chased out of town by armed thugs, and all his calls for assistance, first to the regional governor, and then to the government in Bishkek, failed to restore his control of the factory. When the government finally ordered the police in to retake control of the factory on behalf of the rightful

²¹ See, for example, the World Bank's governance indicators in Kaufmann, Kraay, and Zoido-Lobaton, "Governance Matters II", Policy Research Working Paper 2772.

²² Transparency International Corruption Perceptions Index 2002, available at www.transparency.org.

²³ "Kazakhstani Prime Minister Admits to Existence of Secret Government Fund", *Eurasia Insight*, 5 April 2002, available at www.eurasianet.org/departments/insight/articles/eav040502a.shtml.

²⁴ ICG interview, February 2003.

²⁵ Pauleen Jones Luong, "Political Obstacles to Economic Reform in Uzbekistan, Kyrgyzstan and Tajikistan: Strategies to Move Ahead", p. 17, paper given at Lucerne CIS-7 conference, 20-22 January 2003. Available at www.CIS7.org.

owner, they were forced to retreat by private security guards.²⁶

This inability of the state to assert itself against informal power centres, including mafia groups and powerful business groups, is a major caveat to any investment program in Central Asia. There is simply not a strong enough guarantee that a company can call on the state and the law enforcement agencies to protect its interests impartially. In part, this may be because the state has been infiltrated or undermined by criminal groups or corruption. The close link between state organs and the criminal world has been most notable in Tajikistan, where the lines between criminality and state blurred during the civil war, but there is also a semi-criminal element close to the elites in all Central Asian states, often linked to narcotics trafficking. In Turkmenistan, reliable reports suggest that President Niyazov has personally benefited from drugs smuggling.²⁷ In Uzbekistan, a mafia has reached a compromise with the state that allows it to operate largely unimpeded. Drug cartels have achieved leverage within the security organs of all states in the region.

Dealing with corruption is the number one priority for improving investment in Central Asia. But government anti-corruption programs tend to be mostly for show, or target only political opponents. To really get to the heart of the problem requires political change, more openness in government, a stronger media, and a more independent judicial system. A greater willingness by the international community to tackle this sensitive subject, and to make sure its own companies and projects are not enmeshed in the same system, would also be a positive step.

IV. TRADE, REGIONAL COOPERATION AND GLOBALISATION

Few countries have been as hard hit by the break-up of the Soviet Union as those of Central Asia. Where once no barriers divided the republics, mines, barbed wire and all the institutions of customs and border guards have been introduced. The difficulties involved in moving goods have severely limited intra-regional trade.

The small town of Kara-Suu, twenty miles outside the Kyrgyz city of Osh, is famous for its bazaar. A sprawling territory of containers and stalls, it offers some of the best value goods in Central Asia. A radio-cassette recorder can be had for less than U.S.\$5 (guarantee: one week), and a huge range of clothes, shoes and household goods are sold for bargain prices. The prices are cheap because the goods mostly come from China, over the mountain passes from Urumchi and Kashgar.

The reason the bazaar is in Kara-Suu is its location, close to the big Kyrgyz town of Osh, but also on the border with Uzbekistan. When Uzbekistan restricted bazaar trade inside the country in 2002, hard currency flooded out to buy goods in Kara-Suu, possibly up to U.S.\$2 million a day, according to some local officials. Instead of relaxing its trade restrictions in an attempt to revive business inside its borders, the Uzbek government took a simple decision in December 2002: it dismantled the bridge that links Kara-Suu with the Uzbek bank of the river, at a stroke cutting all legal cross-border trade. In response traders built their own precarious crossings, which were pulled down by border guards. In one case Uzbek border guards opened fire on traders trying to cross the river.²⁸

It is not just the physical barriers of borders that block the free flow of goods. In Kyrgyzstan, sometimes cited as the most liberal of the Central Asian states, an entrepreneur wishing to export fruits or vegetables has to go through at least thirteen different procedures before gaining customs clearance for his goods. This process, which essentially consists of certifying and registering a shipment with various government agencies, is time-consuming and costly.

Things do not get much easier once the process is complete. Despite having all the correct documents in hand, a Kyrgyz driver wanting to enter Uzbekistan is likely to face demands for bribes at several checkpoints and then have to repeat the process on the other side of the border. Needless to say, an

²⁶ See *Slovo Kyrgyzstana* [Bishkek], 3 January 2002; additional information from ICG interviews.

²⁷ See ICG Report, *Cracks in the Marble*, op. cit.

²⁸ "Obstrely Kara-Suu. V chem prichina perestrelki na Kyrgysko-uzbekskoi granitse". *Moya stolitsa* [Bishkek], 18 April 2003. The amateur bridge-builders demonstrated how a liberal border regime could work – they charged five soms (U.S.\$0.1) to get across, plus a scaled tariff for goods; there were no document checks or customs authorities. Similar illegal crossings are available at other parts of the Uzbek border. Occasionally border guards try to stop crossings; more often they turn a blind eye in exchange for bribes.

Uzbek driver going the other way faces similar obstacles from Kyrgyz officials. Shipments across Kazakhstan can be even worse. The Asian Development Bank estimates that transporting a can of tomato paste by road from Bishkek to Novosibirsk (Russia) will add around 35 per cent to the price.²⁹ And this may be conservative. One analyst told ICG that up to 60 per cent of the value of trade contracts between Kyrgyzstan and Russia can go toward paying official and unofficial transport costs while a shipment passes through Kazakhstan.³⁰

The broken bridge of Kara-Suu is symbolic of the failed attempts to bring the Central Asian states together into a trading bloc that would overcome their own individual small markets and attract foreign investors who could serve the whole region. Attempts to revive the fabled Silk Road, an ancient trading route from China to Europe, have led to countless international conferences and EU-funded jamborees. The EU's Transport Corridor Europe-Caucasus-Asia (TRACECA) project has produced colourful maps of future infrastructure that might one day again link the two continents. But these grandiose projects have never come to fruition. The political and economic policies of the Central Asian states have placed too many obstacles in the path of free trade or free movement of peoples across frontiers in the region.

None of these obstacles have any significant impact on illegal cross-border trade. Drugs flow freely across difficult borders. The Central Asian countries combined seized about 4.6 tons of heroin in 2002,³¹ but even conservative estimates suggest that seizures account for only 10 per cent of real traffic. Despite the apparent heavy security presence at many checkpoints, the right connections or the right bribes can enable almost anyone to cross Central Asian borders. The only people who really suffer are the 90 per cent of the population who have neither money

nor connections and merely wish to get their legitimate goods to market.

Successive attempts to sort out borders and improve regional integration have foundered on political objections to regional projects by Uzbekistan and Turkmenistan; on Kazakhstan's rapacious border guards and customs officials; and on Tajikistan's previous failure to clamp down on militant groups that gave Uzbekistan the excuse for the mine fields that now run the length of much of its south-eastern border. But this excuse has now faded considerably. The security situation in Tajikistan is much improved, and the threat from militant groups in Afghanistan has lessened, although it has certainly not disappeared.

The time has come to open up borders again to cross-border trade and movement of people. Achieving this is not easy, partly because the economies of the Central Asian states have diverged significantly over the past decade. But without improved regional trade, none of these economies are likely to see long-term prosperity. The situation is most acute in the complex of undemarcated borders and enclaves in the Fergana Valley. Major parts of the Kyrgyz-Uzbek border remain disputed, and the Kyrgyz-Tajik border is still not officially demarcated along most of its length.

Because of their geography and relative lack of natural resources, Kyrgyzstan and Tajikistan are destined to be trading nations. Prosperity, therefore, depends on their ability to access the markets of China, Iran, Turkey, Russia, and perhaps ultimately Europe. The reality, however, is that, apart from China, access to these markets requires transit through Uzbekistan, Turkmenistan, and Kazakhstan. Some sort of regional trade agreement is thus critical to any model of economic well-being in Kyrgyzstan and Tajikistan.

TRACECA and other regional transport projects, such as EBRD investments in the transport sector, should be reformed to create a coordinated program that would explicitly link any external assistance in transport infrastructure to the acceptance of international norms in border crossing and visa procedures. Tighter border procedures would have to be justified in closely defined national security terms. Independent monitoring groups could be included to ensure compliance. This might mean that countries that restrict trade through closed borders and punitive tariff regimes, such as Uzbekistan and Turkmenistan,

²⁹ International Monetary Fund, Country Report N°03/53, "Kyrgyz Republic: Selected Issues and Statistical Appendix", February 2003.

³⁰ ICG interview, Osh, April 2003

³¹ Figures compiled from country statistics provided by the UN Office for Drug Control (UNODC). There is little likelihood of any fall in transit volumes in the near future. The 2003 UNODC Afghan Opium Rapid Assessment Survey published in March 2003 suggested that opium production in the northern provinces of Afghanistan was expected to show a "large increase" in 2003. Much of this will no doubt be trafficked through the Central Asian states.

would be excluded from such programs. So be it. Any other approach ensures that improved bilateral relations among more cooperative states are held hostage by leaderships who fail to see the need for a regional solution to problems.

V. RESPONSIBLE BUSINESS

Given the lack of foreign investment in Central Asia, almost all capital inflows might be seen as positive. But in several sectors, little attention is paid to the idea of “people prospering”, or indeed of responsible engagement to improve political and social conditions. Foreign investors need to take serious account of how their actions impact on the level of corruption in a state, on the nature of political regimes, and on the lives of ordinary people working in their sectors.

In Turkmenistan, the grandiose buildings that dominate the skyline of Ashgabat have been built almost exclusively by a few Turkish construction companies and the French engineering giant Bouygues. Among other edifices designed to promote the regime, Bouygues is responsible for Niyazov’s presidential palace and a huge mosque in the village where Niyazov was born. It has reportedly also funded investment in Turkmenistan’s state television, a propaganda machine that serves only to perpetuate the president’s cult of personality.³²

Although private investment can serve as an important path to opening closed societies to outside influences, sometimes Western companies attempt at engagement achieve a grotesque level of subservience. On 6 February 2003 the president of Daimler Chrysler Overseas, Erich Jonscher, met with President Niyazov of Turkmenistan and presented him with a German translation of Niyazov’s book, the *Ruhnama*, that had been funded by Daimler Chrysler with no apparent regard for the appalling impact that the volume is having on education and society in Turkmenistan.

In resource-extraction industries, it is easy for governments to control profits with little transparency as to their final destinations. This has been a major problem in the Kazakh oil sector, where

an American middleman, James Giffen, is facing charges of paying massive bribes to Kazakh government officials on behalf of U.S. oil companies. In Turkmenistan much of the profit from the oil and gas sector goes directly into the Foreign Exchange Reserve Fund (FERF), an off-budget account effectively under the personal control of President Niyazov. He has used this fund for personal purposes and for developing the cult of his personality through the construction of statues, monuments and other grandiose projects. The EBRD has suspended investments in any project the profits of which go into the FERG,³³ but many private companies continue essentially to support the dictatorship through their commercial activities. Similar concerns surround Western investments in resource extraction in other Central Asian states.

In addition to feeding corruption and supporting the worst aspects of dictatorial rule, in some sectors little attention is paid to the well being of workers. This situation is common throughout Central Asia in the cotton sector. In Kyrgyzstan and Kazakhstan, cotton farming has largely been privatised, leading to a gradual improvement in farmers’ incomes, and the involvement of a number of foreign companies that provide technical help, futures’ contracts and alternative channels for sales. In Kyrgyzstan an association of cotton-farmers has allowed members to sell to the world market directly for the first time. There are still problems, particularly with treatment of workers in Kazakhstan, but the situation is slowly improving.

The contrast in Uzbekistan, Tajikistan and Turkmenistan is stark. In Andijan province, in Uzbekistan, just across the border from Osh province, young children are sent for up to two months from school to work on the harvest. Farmers are paid a fraction of the world price for the cotton, which is all sold to the state. Regional bosses and criminal groups buy it at cheap prices, siphoning off some for sale at market prices in Kyrgyzstan and Kazakhstan, while most is sold on by two companies to international buyers on behalf of the state. Swiss companies are significant participants in the cotton industry in Tajikistan, where farmers have run up huge debts to international investors under futures schemes.³⁴

³² Turkmen TV first channel, Ashgabat, 23 August 2002, reported by BBC Monitoring Service, Central Asia, 24 August 2002.

³³ “Turkmenistan: Country Strategy”, www.ebrd.org.

³⁴ ICG Report, *Tajikistan*, op. cit. Paul Reinhardt AG is the most significant of the Swiss companies.

Although oil companies have at least partly understood the need for responsible behaviour towards the communities with which they interact, other resource extraction industries seem slow to follow on. The danger is that their actions perpetuate the very conditions that ensure that there is so little foreign investment in the region in the first place and stimulate further disenchantment with the West's role in the region.

VI. WATER: DISPUTES AND COOPERATION

Lack of regional cooperation is perhaps most dangerous over water, a vital resource that is at the heart of much political discord. The failure to regulate this issue has led to the region's most notable ecological disaster, the disappearing Aral Sea, but it also has serious political and economic consequences for the states concerned.

Tensions focus on the two main rivers of the region, both of which flow to the Aral Sea – the Syr Darya from Kyrgyzstan through Uzbekistan and Kazakhstan and the Amu Darya from Tajikistan through Uzbekistan and Turkmenistan. Kyrgyzstan and Tajikistan control the upwaters of these rivers, and the tension between their needs and those of downstream states is a major source of political discord. There is also tension among downstream states. Disputes over water use between Turkmenistan and Uzbekistan nearly led to military confrontation in 1995, and the collapse of talks in late 2002 does not augur well for the future.

The Amu Darya and its tributaries form part of the border between the Central Asian states and Afghanistan, and increased demand from Afghanistan for water will merely exacerbate the problem. Currently that country uses very little of the flow from the Amu Darya but reconstruction of irrigation systems will put additional pressure on the river.

The economies of Uzbekistan and Turkmenistan are highly dependent on intensive irrigation for crops such as cotton and rice. But irrigation systems have decayed so severely that, due to filtration and evaporation, half of all water never reaches the fields.³⁵ The downstream countries require more

water for their growing agricultural sectors and rising populations, while the economically weaker upstream countries are trying to win more control over their resources and want to use more water for electricity generation and farming.

Management systems are in place to regulate water use but they have generally failed to address the real issues. The Interstate Coordinating Water Commission (ICWC), set up in 1992, has not taken into account changing political and economic relations. It is an inter-governmental body with little transparency that focuses almost exclusively on the division of water. There is no representation from agricultural or industrial consumers, non-governmental organisations or other parties.

Western donors have started to develop other management systems such as the Global Environment Facility (GEF) program, in coordination with the International Fund to Save the Aral Sea (IFAS). The UN-backed Special Program for the Economies of Central Asia (SPECA) is also working on water management. However, none of these initiatives have made much headway in dealing with the key political obstacles, particularly the unwillingness of the states to cooperate.

In general, international involvement in the water sector has seen more failures than successes. High-cost technical programs involving foreign specialists have usually failed to understand the local specifics of water management traditions and the political context in which they operate. One review of international aid to the water sector asserts that "USAID ... spent tremendous funds... giving little attention to effectiveness, practicality and outcomes".³⁶ Many other donors have been equally profligate and ineffective.³⁷ Lack of results has tended to limit assistance to the sector, with donors wary of putting more funds into what is often seen as a black hole.

The initial focus by international agencies on expensive technical fixes to the water problem often matched the preference of Central Asian nations to approach the issue purely as an

³⁵ See ICG Asia Report N°34, *Central Asia: Water and Conflict*, 30 May 2002.

³⁶ V. A. Dukhovny, "Ten Years of Donor Support for the Aral Sea Basin Program", paper presented to the Asia Development Bank (ADB) Regional Workshop, "Cooperation in Shared Water Resources in Central Asia: Past Experiences and Future Challenges", Almaty. 26-28 September 2002.

³⁷ *Ibid.*

engineering problem rather than one of managing multiple political, social and economic factors. There is now a much wider understanding among experts that the water issues of the Aral Sea basin can hardly be tackled without raising related issues of social and economic policy. However, getting this understanding accepted by key decision-makers is more difficult, because of the strength of powerful lobby groups, particularly those with vested interests in increasing cotton production without paying the real costs of irrigation.

A typical example of this approach is Uzbekistan's support for the diversion of Russian rivers to Central Asia to address the water deficits in its agricultural regions. Such a project is not commercially viable and is likely to be accompanied by major environmental consequences. For the Uzbek government, however, such an approach is attractive since it avoids the need to rethink an agricultural policy that continues to emphasise state-controlled cotton production and is weighted against the kind of private farming that would be necessary to encourage payment for water usage and efficient irrigation.

More effective international programs have sought to increase low-level, grass-roots support for alternative water management and have begun to include NGOs and private farmers in decision-making on water use. Such a low-level approach is useful and necessary, but there is still a major need for overall political coordination among the Central Asian states to produce a multifaceted approach that addresses energy, agriculture and demographic aspects of water use. Management of water needs be reformed to increase accountability and transparency and begin to include price mechanisms that will encourage efficient use. But above all, political leaders need to take difficult decisions that tackle vested interests in the agricultural sector and accept the need for compromises with neighbours.

VII. NURTURING SMALL BUSINESSES

The Soviet legacy was always going to make developing the private sector difficult. Too many government officials continue to think in terms of grandiose economic projects in which the state has a leading role. And the concept of the state interfering in business remains widely accepted. Yet, despite the problems, entrepreneurship has spread quickly. As

the old system collapsed, people found new ways to survive, usually through setting up small private enterprises, mostly in trade, but increasingly in services and sometimes production. This obvious willingness of the population to engage in business – and the skill of many Central Asians in the age-old tradition of trading – has not been matched by government policies designed to encourage this sector.

Kazakhstan and Kyrgyzstan have been the most progressive in terms of economic reform and liberalisation. Kyrgyzstan, for long the darling of the international financial institutions (IFIs), has been clever at playing the international community, and particularly good at presenting itself as a democratic, reforming partner in an otherwise difficult region. But behind the fine words and international conferences, much of the political system and economy is mired in corruption, and ambitious plans announced at international gatherings do not always turn into reality on the ground.

Nevertheless, with all its problems, Kyrgyzstan is beginning to make some slow moves forward. Privatisation of agriculture was initially a disaster in many areas, as farmers sold their cattle for money rather than invest for the future. But now, in some areas, private agriculture is beginning to pick up. In 2002 agricultural exports were up 30 per cent, and new schemes for farmers in southern Kyrgyzstan are leading to possible exports of fruits, vegetables and flowers to Russia, Europe and elsewhere. Most of these schemes are still a long way from fruition, but at least tobacco and cotton are now exported privately.

In Kazakhstan growth of small and medium sized enterprises (SMEs) has picked up on the back of oil development, and there is a much greater element of SME involvement in the service sector. The danger for Kazakhstan is over-investment in the oil sector at the expense of other economic areas. Oil reserves are projected to run out in 2015,³⁸ meaning the country will have to rely increasingly on SMEs in other sectors if growth is to continue. However, in the agricultural sector, for example, much-needed land reforms are proceeding only slowly, and a draft land code would leave a number of limitations on private ownership. With an estimated 43 per cent of the population living in the countryside,³⁹ these

³⁸ Economist Intelligence Unit (EIU), "Kazakhstan Country Report", April 2003.

³⁹ Ibid, January 2003.

reforms are essential if agri-business is also to contribute to future growth.

In the other three states, the situation of SMEs is considerably worse. Turkmenistan's private sector is limited and under constant pressure. Though the government claims that the private-sector accounted for 40 per cent of the country's GDP in 2002, that figure is probably significantly inflated.⁴⁰ Investment is mostly concentrated in the energy and construction industries, both of which are characterised by heavy state involvement. Already the least attractive in Central Asia, Turkmenistan's investment climate is unlikely to improve as long as President Niyazov remains in power.

In Uzbekistan, which has perhaps the greatest potential for SME development, the government has rhetorically backed small business, and the Ministry of Justice has attempted to clamp down on interference by local government. In reality, though, business has little independence. Every official, from the head of a *mahalla* (local government committee) to the presidential administration continues to feel the right to intervene largely at will in its affairs.

A huge blow to the whole private sector was dealt by the trade restrictions introduced in Uzbekistan in 2002. The number of SMEs involved in trade and distribution dropped sharply as a result.⁴¹ Many business-people have had their goods confiscated in the aftermath of the new regulations; others have been forced into semi-criminal contraband activities; and corruption among customs and regulatory authorities has grown as a result. Further hard to justify regulations and controls on small business continue to appear regularly.

It is not just official government regulations that damage SMEs in Uzbekistan. There are many reported cases of thriving businesses being seized or bought up cheaply by government officials. Businessman Olimjon Yusupov alleges that his successful bread-making company was taken over illegally by relatives of a high-ranking government minister in 2001, after a court was persuaded to annul his ownership rights.⁴² Yusupov complains:

On the one hand they all talk about support for small and medium sized business, and at the same time you get this complete disregard for the law on the part of official members of the government. The law is on my side, but for [the government minister named] the law does not exist.⁴³

This is not a one-off case. The same minister is alleged to have built up a major portfolio of property and businesses using similar methods of illegal pressure on business people and abuse of courts. There is little recourse to justice for such individuals, despite the rights to property embedded in the constitution.

Tajikistan's SME sector is small, employing only about 1 per cent of the workforce according to official statistics.⁴⁴ The same obstacles of corruption, government interference, complex tax regulations and bureaucracy have kept growth in this sector limited. Indeed, until 2001 inspectors apparently outnumbered business-people.⁴⁵ Since then business leaders have achieved some cuts in the inspection agencies, but even so small businesses are frequently the targets of predatory raids, usually without any justification. Again, government attempts to set up complaint hotlines or other mechanisms to defend SMEs seem to have little impact.⁴⁶

A common problem in all the Central Asian states is that leaderships tend to see the private sector as a potential threat to their political power. The example of Kazakhstan, where private business-people have been at the centre of a well-funded opposition movement, has not gone unnoticed. In Kyrgyzstan, business-people have been co-opted by the political elite, or forced out of business if they threatened to support political opponents. In Uzbekistan the fear of an independent business class emerging has been one reason for the constant stream of decrees that enforce government control over many business sectors. High levels of government regulation make businesses very dependent on the state authorities: any sign of activity that might be deemed dangerous for the government can be stopped through simple

⁴⁰ EIU, Turkmenistan Country Report, March 2003.

⁴¹ "Number of trading entities drops in Uzbekistan", Uzbek TV report, first channel, 5 April 2003, in BBC Monitoring Global Newswire Economic File – Central Asia, 6 April 2003.

⁴² S. Ezhkov, "Kapkan, ili nadezhda umiraet posledney", Pravda vostoka, 22 August 2002.

⁴³ ICG interview, Olimjon Yusupov, Director, "Kavsar Fidoiv", Tashkent, April 2003.

⁴⁴ The real figure may be higher because of the informal nature of large parts of the SME sector but it is clearly still low. See Economist Intelligence Unit, "Country Report", March 2003, p. 23.

⁴⁵ Ibid., p. 34.

⁴⁶ See ICG Report, *Tajikistan*, op. cit.

threats to remove licenses or carry out a tax inspection.

In such systems it is difficult to achieve SME growth without challenging the perceived political security of the elite. Commendable schemes, such as SME credit lines promoted by international financial organisations, are important mechanisms to encourage business growth, but they are often less effective than advocacy with governments to take down the regulatory barriers that block growth. The EBRD's SME credit lines in Uzbekistan are a useful support for the private sector, but the U.S.\$180 million provided since 1996 is far less in money terms than small business people have lost over the past six months in Uzbekistan as a result of misguided government policies.⁴⁷

To achieve rapid SME growth, the Central Asian states need to start taking down barriers – technical and political – and accept that a rising middle class will eventually want a greater political say. The whole array of Western assistance programs to SMEs, from the U.S. Pragma program to IFI credit lines, will not be effective unless pressure can be brought to bear on governments to challenge corrupted and predatory institutions that block economic growth. Support for SMEs needs to be linked much more closely to high-level political advocacy by governments and international institutions and also to support for individual businesses to group together and organise their own pressure groups.

Business people need to be able to build up their own advocacy and lobby groups, and feel free to put pressure on government authorities from below. Under present political realities, they are unlikely to form a powerful political force unless governments are persuaded that an active business sector, independent of government, is essential for economic growth.

VIII. CONCLUSION

The former Soviet states of Central Asia historically formed the heart of Inner Asia, acting as a major trade route between East and West, North and South.

⁴⁷ In October 2002 Kazakh officials claimed that U.S.\$4 million per day was leaving Uzbekistan for shops and bazaars in southern Kazakhstan, as a result of new trade restrictions. ICG interviews, October 2002.

They could take up that role again, boosting trade across the region from China to Iran, Russia, Pakistan and Turkey, and offering their important resources, both natural and human, as a major force in that wider region.

So far though, optimistic prognoses, prevalent in the euphoria of the early independence years, have failed to come true. Only Kazakhstan has achieved any real economic progress that has had a positive impact on people's lives. In the rest of the region, much of the population dreams mainly of emigration to richer nations. Young people see few prospects for advancement under present political and economic realities. Governments seem unable to adjust to the realities of globalisation and incapable of meeting the rising demands of growing populations.

The role of the international community in Central Asia has not been entirely beneficial. Investors and international agencies must take some responsibility for the widespread corruption that has emerged as a common theme in the governance of the region. Bilateral relations have too often been dominated by geopolitical and commercial concerns; Western states have too seldom been willing to challenge the status quo or speak out about political repression or high-level corruption. The result has been profound disappointment with the West in much of the region, growing disenchantment with democracy as a political system, and, in some instances, growth of Islamist sentiment as an alternative political and social order.

The EBRD is no exception to this mixed record for international engagement in the region. Its decision to hold its Annual Meeting in Tashkent demonstrates a commitment more to maintaining good relations with governments than to its founding principles. But it now has a chance to act as a catalyst for the international community by taking a tougher line on economic and political reform and making further funding much more contingent on real progress.

Uzbekistan is the heart of Central Asia, and its policies have a profound impact on the stability and economic prosperity of its neighbours, particularly Tajikistan and Kyrgyzstan. An emphasis on reform there should not cloud the need for positive change in other Central Asian states. But Uzbekistan offers the greatest potential, both for region-wide positive economic benefits, and also for serious instability if its political and economic systems continue to fail its people.

Hence the need for a serious focus on the prospects for reform in Uzbekistan and much greater willingness by the international community to apply real pressure to make it happen. The EBRD has adopted a new country strategy for Uzbekistan that emphasises political change and increased economic reform. The strategy outlines a number of areas where the EBRD expects change, on human rights, and on economic policy.

The key issues are those that most of the international community accept, including an improvement in human rights, particularly a serious commitment to fulfil the UN Special Rapporteur's recommendations on torture; opening up the political system, with freedom for human rights groups and political groups to organise; and increased freedom of the press and media.⁴⁸

In economic affairs, liberalisation of the foreign exchange regime remains a priority in the EBRD strategy, in addition to government commitments to reform of agriculture made under the IMF agreement of 2002; improvements in the trade and business environment; reform of the banking system, and cuts in subsidies in the energy sector. Failure to achieve these benchmarks will lead to a review of the EBRD strategy, and possible downturns in lending.⁴⁹

The EBRD country strategy is a commendable attempt to apply political conditions to an international financing program. But the danger is that this strategy will be just another platitude, implemented inconsistently and without any serious commitment by the government. The EBRD needs to state publicly that the Annual Meeting in Tashkent is not a mark of approval for Uzbekistan's economic policies, as it is being presented in the Uzbek media, but rather a last chance for change.

The timetable for that change needs to be speeded up. The Bank has asserted that the strategy will be reviewed in one year: a shorter timeframe is quite feasible. Some EBRD conditions, such as registering human rights groups, are not difficult. It is as easy

for the government to do them now, as in 2004. The EBRD should provide regular quarterly public briefings in Tashkent and London on how it considers the government is doing with the benchmarks.

Further funding needs careful conditioning. The size of a third SME credit line should be explicitly linked to concrete improvements in the SME business environment, including liberalisation of the foreign exchange regime. If the business environment worsens, the Bank needs to consider whether even SME credit facilities are really beneficial in light of active government opposition to business growth.

Funding for the transport sector needs to be reviewed seriously in light of Uzbekistan's failure to match the spirit of agreements under the TRACECA program. There should be no new funding for transport initiatives without commensurate changes in border regimes.

To gain support for a major reform push, the EBRD also needs to work more closely with other organisations, such as the Organisation for Security and Cooperation in Europe (OSCE), to put political pressure on the government. The EBRD should also make the government aware that it will carefully consider monitoring efforts by NGOs and other groups when it assesses performance.

Governments with interests in the region also need to play a stronger role. The EU has failed to make any serious political impact in Central Asia, and its member-states are often too concerned about narrow commercial interests. EU member-states are generally weak in addressing human rights concerns or making strong political representations to governments. The United Kingdom has begun to take a stronger line in the past twelve months, but it would be more effective if EU member-states could present a stronger united front on key issues.

The U.S. has a particularly important role to play with its increased military and political presence in the region. With Uzbekistan it has developed a close security and military relationship, but these links need to be matched by public pressure for reforms in politics and economics. The U.S. and Uzbekistan have signed a far-reaching Declaration on Strategic Partnership and Cooperation that outlines in some detail a series of commitments by Uzbekistan to reforms in the political system, the economy and the justice sector. Unfortunately, one year on, almost nothing has been implemented. Yet, in the latest

⁴⁸ Uzbekistan's record on press freedom is very poor. According to the Freedom House ratings for 2000, only Turkmenistan, Saudi Arabia, Burma (Myanmar) and Cuba had worse records. UNDP, *Human Development Report* (New York, Oxford, 2002), p. 39. During 2002, however, there was some slight relaxation, with the abolition of formal censorship and the appearance of occasionally critical articles in some papers.

⁴⁹ The country strategy is available on www.ebrd.org.

statement on U.S.-Uzbekistan relations, released in April 2003, the “United States appreciated the measures being taken by the Government of Uzbekistan to further implement political reforms and establish the institutions of a civil society”. It is not clear what these measures are, and the rest of the document only hints at slight U.S. dissatisfaction with progress on reform.⁵⁰

This kind of language is no longer tenable. Positive engagement and constant concessions to the government have produced very few results for the population. The West, and the U.S. in particular, threatens to discredit itself through its too close relationship with dictatorial Central Asian regimes. A first step would be agreement among the OSCE, the EU, the U.S. and the EBRD on a number of fundamental reforms that are vitally needed in Uzbekistan, with a joint public statement made after the EBRD Annual Meeting that outlines the public position of these key players.

In most cases Central Asian states have been largely free of serious political violence over the last decade. But complacency would be misplaced: the underlying currents of economic discontent and social upheaval, and the influence of radical Islamist groups are very real if not always visible. Many of these heavy-handed governments are essentially weak in terms of legitimacy and functioning state organs. Lack of political and economic reform threatens not just prosperity and freedom for the peoples of the region, but long-term security in Central Asia.

At a time when the West’s reputation in the Islamic world is of paramount importance, more attention should be paid to the needs of the people of Central Asia and rather less to their often self-serving and oppressive governments. The international community, and the West in particular, is in danger of discrediting its presence in the region by its lack of pressure on the region’s dictators. Delegates to the EBRD Annual Meeting need to make the event the start of a new process of real positive change; otherwise it will become merely one more instance of the international community legitimising an oppressive regime and undermining the region’s prospects for peaceful political and economic development.

Osh/Brussels, 29 April 2003

⁵⁰ Press Statement, “United States–Uzbekistan Joint Security Cooperation Consultations”, Washington, D.C., 15 April 2003. Available at www.state.gov.

APPENDIX A

KEY FACTS AND FIGURES

Economic indicators

	GDP per capita (U.S.\$) 2002	Real GDP Growth 1999	Real GDP Growth 2000	Real GDP Growth 2001	Real GDP Growth 2002	FDI ⁵¹ per capita (U.S.\$) cumulative end-2000
Kazakhstan	1,649	2.7	9.8	13.2	9.5	564
Kyrgyzstan	327	3.6	5.0	5.3	-0.5 ^a	92
Tajikistan	170	3.7	8.3	10.2	9.1	30
Turkmenistan	2,278 ^b	16.9	17.6	20.5	21.2	176
Uzbekistan	305	4.1	4.0 ^a	4.5 ^a	4.2 ^a	37

Source: Economist Intelligence Unit; ^a government figure; ^b at official government exchange rate

Political/Economic development

	Freedom House 2002 Combined Political Rights and Civil Liberties Rating (1-7, with 7 denoting least freedom)	Heritage Foundation / <i>Wall Street Journal</i> 2003 Index of Economic Freedom (out of 156 countries)	United Nations Human Development Index 2002 (out of 173 countries)
Kazakhstan	5.5	119	79
Kyrgyzstan	5.5	104	102
Tajikistan	6.0	143	112
Turkmenistan	7.0	146	87
Uzbekistan	6.5	149	95

⁵¹ Foreign Direct Investment

Political leaderships

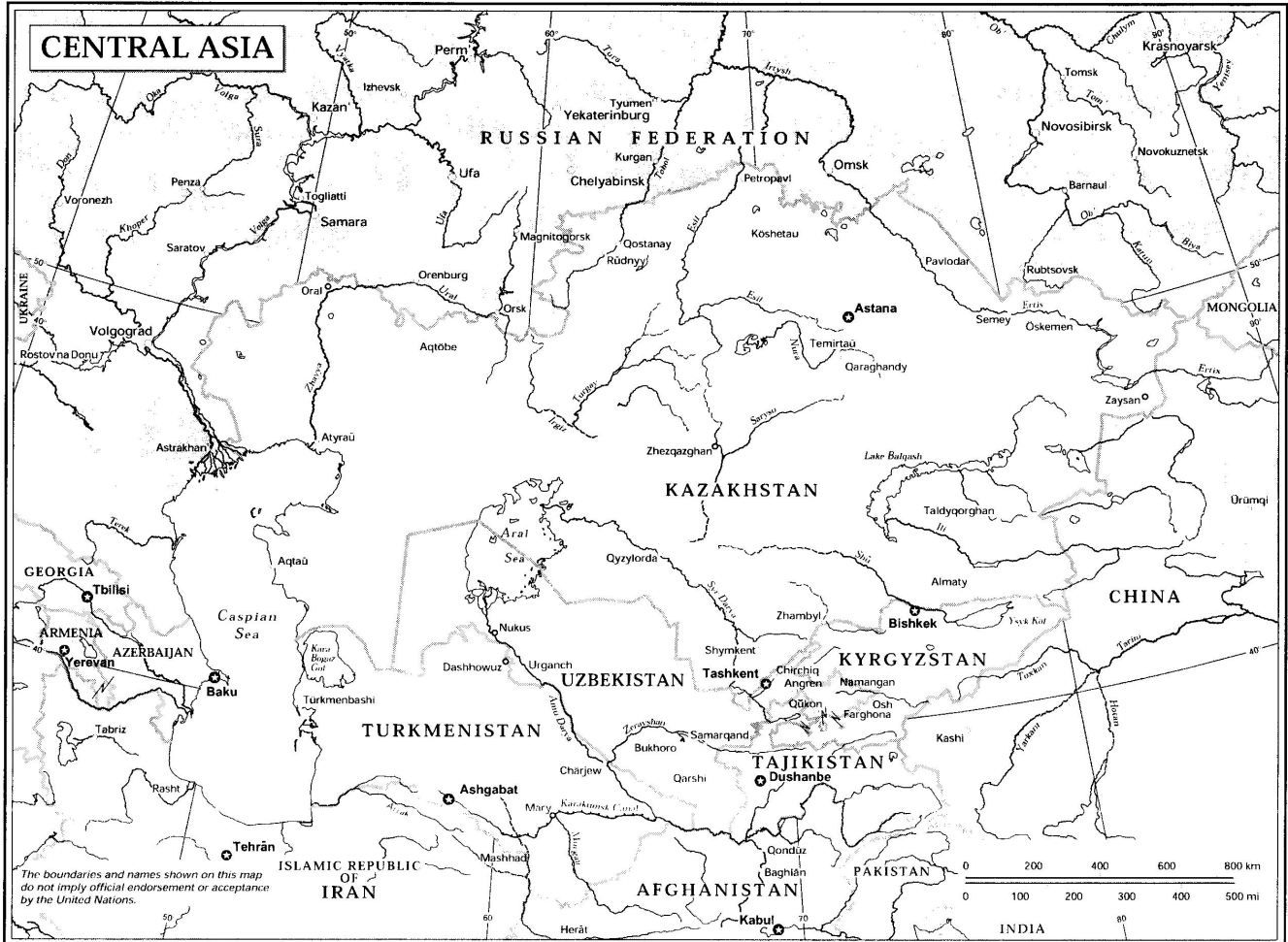
	President	Came to Power	Next Election	Age
Kazakhstan	Nursultan Nazarbayev	1989	2006	62
Kyrgyzstan	Askar Akayev	1990	2005	58
Tajikistan	Imomali Rakhmonov	1992	2006	50
Turkmenistan	Saparmuryat Niyazov	1985	-	63
Uzbekistan	Islam Karimov	1989	2007	65

Demographics

	Population 2000 (millions)	Projected Population 2015 (millions)	Annual Population growth rate 1975- 2000 (per cent)	Population under age 15 (2000)
Kazakhstan	16.2	16.0	0.5	27.0
Kyrgyzstan	4.9	5.8	1.6	33.9
Tajikistan	6.1	7.1	2.3	39.4
Turkmenistan	4.7	6.1	2.5	37.6
Uzbekistan	24.9	30.6	2.3	36.3

APPENDIX B

MAP OF CENTRAL ASIA





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