Chapter Three

SOME ECONOMIC DIMENSIONS OF SECURITY IN CENTRAL ASIA AND SOUTH CAUCASUS

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INTRODUCTION

What are the economic dimensions of destabilization of a society? Under what economic conditions is the political and social order likely to be subjected to radical change, widespread internal disorder or major external violence? Regrettably, neither the general question nor its application to Central Asia and South Caucasus can be answered with confidence. The links between the economic and the political-social orders are too complex—both the direction of causation and the forms of the functional relations are often ambiguous—for prediction without extensive qualification.[1] This seems particularly true in what may be the early stages in the development of a long-term U.S. and allied presence in Central Asia.

This analysis begins with a general discussion of the principal economic connections to societal destabilization. The main, second section elaborates the application to CASC of two of the most important links. A final section examines the regional prospects, especially in the new, post-September 11 context.

There is a first-order distinction between exogenous and endogenous sources of destabilization, but the two may interact in various ways, in which the political-strategic and the economic intertwine. For example, the penetration of armed forces from outside the coun-

[1]It might appear that the effect of political instability on economic growth is intuitively clear and negative, but Nauro Campos and Jeffrey Nugent ("Who's Afraid of Political Instability?" William Davidson Institute Working Paper, No. 326, July 2000) show otherwise.

try represents the most obvious exogenous source of security disruption. In turn, the armed encroachment may trigger internal upheavals resulting from pre-existing faultlines in the society, or the latter may be the pretext for or magnet drawing the external incursion (e.g., Islamic militant activities in Central Asia in recent years).[2] The ability of the affected governments to cope with such intrusions will depend heavily on the size, character, and skill levels of their armed forces, which are shaped in part by the magnitude and distribution of military budgets. In the long run, budgets depend on the size of the economy, but in the short run they also hinge on noneconomic factors, including politics and social structure.[3]

International trade and finance are the economic links between the external and domestic arenas. Trade can and most often does bring economic benefits in lower prices, higher quality, and greater variety of goods and services, as well as gains in income and employment. But trade may also hinder broad economic progress—and hence may threaten social and political stability—in several different ways.[4]

1. High levels of participation in trade (measured by trade values as a proportion of GDP) can also mean high exposure to price fluctuations in regional and world markets. To the extent that primary commodity markets experience greater price volatility than those for industrial goods and services, primary product exporters, who are also likely to be importers of industrial goods, can suffer from instability of their export revenues and rigidity of their import costs. This double handicap will lead to instability in foreign exchange reserves and government revenues, not to speak of downward pressures on domestic production, income, and employment.

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[2]External factors may support particular factions in internal conflicts or one state in conflict with another, without actual invasions by armed forces. The alleged involvement of Russia in the Georgian civil war in the early 1990s and in the assassination attempts against Georgia's President Shevardnadze in later years form prime examples of the first case. A prominent example of the second is Russia's arms supply to Armenia, which Azerbaijan has continually protested.

[3]Discussed in greater detail in Chapters Two and Four of this report.

[4]The first four numbered paragraphs below adapt, with thanks, material suggested by Tanya Charlick-Paley and Sergej Mahnovski.

2. When resource extraction conducted largely by multinationals is the main source of primary product exports, large-scale repatriation of profits may deprive the economy of much-needed investment and thus help perpetuate low-income status. The oil and gas producers in the Caspian region are aware of that danger, and their exploration and development contracts with the multinationals have been drawn to siphon off a good share of the expected financial returns. It is another matter altogether whether that share ends up in productive and efficient investment or in the maintenance of a repressive, corrupt regime. All too often, natural resource producers act largely as "rentier" states, sustaining the nondemocratic status quo by placating the population with low taxes and enhanced public spending but stifling dissent.[5]

3. Energy development through multinational export attracts foreign direct investment, but it is often not a suitable vehicle for diversification of the industrial structure. Most developing countries look to manufacturing to provide a more complex division of labor and higher standards of living, and there are few forward and backward linkages from primary exports to manufacturing. Azerbaijan and Kazakhstan are now setting up so-called oil funds to accumulate proceeds from energy development and direct them to other sectors of the economy.

4. Natural resource export booms have been linked to output declines in traditional export sectors like agriculture and nonextractive industry via the mechanism of the "Dutch disease." This is a coinage of the 1970s that refers to the deleterious effects on the Dutch economy of significant gas discoveries in the North Sea. The surge of oil or gas revenues threatens appreciation of the country's real exchange rate, as inflows of foreign currency reduce its price, and domestic price inflation through growth of the money supply. Both effects tend to raise the supply prices of nonresource exports and lower domestic prices of competing imports. This can lead to reduced competitiveness of nonresource exports and therefore to decline in the economic for-

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[5]Hazem Beblawi and Giacomo Luciani, *The Rentier State*, London: Croon Helm, 1987, and Terry Lynn Karl, *The Paradox of Plenty*, Berkeley, CA: University of California Press, 1997.

tunes of agriculture and nonextractive industry.[6] One purpose of the oil funds mentioned earlier is to prevent infection from "Dutch disease" by segregating export proceeds and infusing them into the economy gradually over time.

5. Finally, excessive dependence in external economic relations—the concentration of trade in few commodities or with few partners, or investment and credit relations with particular sources—may create vulnerabilities to external influence and pressure that could pave the way to destabilization.[7] All the CASC states have high trade participation rates. Their trade is characterized by strong concentration in two or three commodity categories and, for several of the states, major reliance on a small number of trade partners.

In the category of mainly endogenous sources of destabilization, two sets of conditions, poverty and economic disorder, merit attention. Poverty does not necessarily generate instability, nor does relative affluence guarantee internal peace. Poverty and general economic dissatisfaction under authoritarian regimes may be indefinitely stable, as long as the regime is not confronted by powerful external threats, retains its cohesion, self-confidence, and a monopoly of force, and exercises tight controls on political participation (see Chapter Two). As Tocqueville taught us, authoritarian regimes tend to get into trouble when they liberalize.

In the turbulent corner of Central Asia where Kyrgyzstan, Tajikistan, and Uzbekistan intersect, the threat to the three governments develops from the combination of high unemployment, income levels at or below subsistence, and the challenge of insurgents with political Islamic ideologies. An especially heady ingredient of the radical message appeals to the generally perceived sense of the moral deterioration of society, with governments viewed as the prime source of the corruption. Even Turkmenistan's unchallenged president has

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[6]See also Karl, *The Paradox of Plenty*.

[7]A special case of trade dependence is the availability of only one or two transport routes for landlocked countries. Armenia, for example, depends heavily on transport through Georgia to the latter's Black Sea ports; the only alternative is overland through Iran. Georgia apparently charged Armenia higher freight tariffs than it did Azerbaijan. *RFE/RL Newsline*, V:125, July 2, 2001.

been sufficiently concerned about possibilities of internal unrest to provide the population with free gas, water, energy, and salt, "subject to generous limits on usage and a highly subsidized price thereafter." The price of bread is regulated, and families with per-capita incomes below the official average wage receive a free allowance of flour.[8]

Poverty becomes especially difficult to endure when people become aware of great inequality in the distribution of income and wealth. This perception of deprivation, relative to other social groups within the society or to counterparts in other countries, can be destabilizing. Economic measurement of inequality may point to the potential for trouble, but it is not the magnitude of the deprivation alone that will determine the likelihood and scale of the possible instability. Again, political-social factors are important determinants (see Chapter Two).

Poverty and external debt dependence can be interrelated. The need for higher outlays on poverty-reduction programs may bump up against a weak fiscal revenue base, possibly leading to the financing of budget deficits by external borrowing. Over time, the growing burden of debt service on the budget can reduce the scope for spending on domestic programs. This was the case in both Georgia and Kyrgyzstan.[9]

Economic disorder may be viewed as having two components. *Macroeconomic disturbances* encompass high rates of inflation, severe market imbalances (goods shortages and shopping queues), high levels of wage arrears, or waves of labor strife. What has come to be called *misgovernance* of economic institutions is popularly identified with large-scale corruption and economic crime (see Chapter Four), but it also includes inadequately defined property rights and protections for investors, unregulated financial markets, etc.

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[8]IMF, *Turkmenistan: Recent Economic Developments*, Staff Country Report 99/140, December 1999, pp. 12 and 30.

[9]IMF and World Bank, *Armenia, Georgia, Kyrgyz Republic, Moldova, and Tajikistan: External and Fiscal Sustainability—Background Paper*, February 6, 2001. Hereafter in the notes, this source is designated "IMF/World Bank, February 6, 2001," to distinguish it from the companion piece with the same title except for the words "Background Paper" and dated February 7, 2001. This latter piece is designated "IMF/World Bank, February 7, 2001."

Each of the states under review experienced high rates of price inflation—in some cases, hyperinflation—in the early to middle 1990s. All of them managed to bring inflation under some degree of control with strict monetary and fiscal policies. High inflation persists in Tajikistan and Uzbekistan,[10] and problems of wage arrears and labor discontent are evident in several states of the region, but macroeconomic disturbance is not otherwise a significant feature of the current economic landscape. This does not, of course, mean that such problems will not reappear in the near future.

Misgovernance, in contrast, is a conspicuous and painful condition of the economic life of all the countries of the region. Each has a large "second economy," high levels of public and private corruption, and, a factor closely connected to the previous two, varying but still far from complete transitions to market institutions. Popular perception of widespread corruption undermines the legitimacy of the regime, and corruption, if unchecked, can metastasize to the point of throttling the "first" economy. Paradoxically, attempts to stamp out corruption can be destabilizing too. Because informal economic activities are only quasi-legal or even outright illegal, they almost inevitably depend for their functioning on corruption of local and national authorities. The corruption is likely to be the rule rather than the exception where policing forces are badly underpaid. If the authorities then attempt to siphon off ill-gotten gains of the shadow economy and excise the corruption, the reactions may be violent, particularly if there are well-rooted protection networks in place (see also Chapter Four).

The assertion of misgovernance is clearly warranted, but the scale of the threat to the political-social order is difficult to assess. Several commercial firms and nongovernment institutions have developed and published quantitative indicators of governance,[11] but they may provide misleading comparative evidence on the vulnerability of the states of the region. Ultimately, the stability of misgovernance

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[10] *Monitor* (Jamestown Foundation), VII:53, March 16, 2001, and VII:172, September 20, 2001.

[11] Daniel Kaufmann, Aart Kraay, and Pablo Zoido-Lobaton, "Aggregating Governance Indicators," Policy Research Working Paper, No. 2195, World Bank, October 1999; "Toward More Operationally Relevant Indicators of Governance," PREM Notes, No. 49, World Bank, December 2000.

depends far less on its absolute size, however defined, than on the national political-social structures. The next, main section of this chapter is therefore limited to discussion of two principal issues, poverty and external economic dependence.

REGIONAL OVERVIEW

Two preliminary remarks seem necessary. First, the weaknesses of national statistical systems in CASC suggest strong caution in interpreting the data presented here. In all cases they should be viewed as indicative only, not as precise measures of the magnitudes they describe.

Second, treatment of the eight CASC states as a single region does some violence to the reality. Tables 3.1 and 3.2 display considerable variation among the eight in important demographic and economic parameters of development. To offer only a few examples: Kazakhstan is 90 times the size of Armenia in area and 15 times as large as the three South Caucasus states combined. Uzbekistan's population is six times that of Armenia and 1.5 times that of the South Caucasus states combined. On the other hand, Armenia's degree of urbanization is almost twice as high as Uzbekistan's. In some demographic respects, the South Caucasus three are more like each other than they are like the Central Asian five. Urbanization is higher, fertility lower, infant mortality lower, and life expectancy higher in the former than in the latter group. The economic differences between the two groups of states are, however, less clear.

Poverty

Evidently, these are all poor states. A decade ago, their education, health, and welfare standards exceeded those of their non-Soviet neighbors, but the Central Asian states especially fell below the average income and welfare levels of the Soviet Union. All the CASC states depended heavily on subsidies from the union budget, artificially low prices for energy and raw materials, and planned direction of trade within the Soviet Union. The dissolution of the Soviet Union disrupted trade links, sharply reducing interrepublic trade flows. Exposure to world market prices revealed the hollowness of valuations at administered prices and therefore the noncompetitiveness of

Table 3.1

Central Asia and South Caucasus: Demographic Indicators, 1999

	Armenia	Azerbaijan	Georgia
Total population, millions	3.8	8	5.5
Urban population, % of total	70	57	60
Fertility rates, births per woman	1	2	1
Infant mortality/1,000 live births			
At birth	14	17	15
Age 5 and below	18	32	20
Maternal mortality/100,000 live births	33	43	N/A
Life expectancy at birth, years	74	71	73

	Kazakh-stan	Kyrgyz-stan	Tajiki-stan	Turkmeni-stan	Uzbeki-stan
Total population, millions	14.9	4.9	6.2	4.8	24.4
Urban population, % of total	56	34	28	45	37
Fertility rates, births per woman	2	3	3	3	3
Infant mortality/1,000 live births					
At birth	22	26	20	33	19
Age 5 and below	28	38	34	45	29
Maternal mortality/100,000 live births	N/A	6[a]	N/A	N/A	35[b]
Life expectancy at birth, years	65	67	69	66	70

[a]1997.

[b]2000.

N/A = information not available.

SOURCES: World Bank, World Development Indicators database, except: Armenia, maternal mortality, from Republic of Armenia, *Interim Poverty Reduction Strategy Paper,* March 2001, p. 20; Azerbaijan, infant and maternal mortality, from *Azerbaijan Economic Trends,* January–March 2001, p. 140; Uzbekistan, infant and maternal mortality, from *Uzbekistan Economic Trends,* January–March 2001, p. 92.

Table 3.2

Central Asia and South Caucasus: Economic Welfare Indicators, 1999

	Armenia	Azerbaijan	Georgia
1. Government social outlays			
A. Per head, $			
Education	19	24	11
Health	7	6	5
B. Percent of GDP			
Education	4	4	1
Health	1	1	**
2. Physicians per 10,000 pop.	34[a]	36	N/A
3. Hospital beds per 10,000 pop.	67[a]	90	48[b]
4. GNI per head, $	490	460[c]	620
5. Average monthly wages, $	38	45	33
6. Poverty rate, % of population	44/55[d]	60[d]	60[d]
7. Income inequality, Gini coeff.	0.59	N/A	0.53
8. Human development index, rank among 174 countries†	93	90	85

	Kazakh-stan	Kyrgyz-stan	Tajik-istan	Turkmen-istan	Uzbek-istan
1. Government social outlays					
A. Per head, $					
Education	44	10	3	14	14–56
Health	25	6	2	22	4–18
B. Percent of GDP					
Education	4	2	2	5	9
Health	2	4	1	3	3
2. Physicians per 10,000 pop.	34	N/A	21		
3. Hospital beds per 10,000 pop.	73	N/A	68	N/A	N/A
4. GNI per head, $	1250	300	290	670	720
5. Average monthly wages, $	94	25	10	62	66
6. Poverty rate, % of population	N/A	64	83		
7. Income inequality, Gini coeff.	N/A	0.43/0.37	N/A	62[e]	N/A
8. Human development index, rank among 174 countries†	N/A	98	115	100	106

†Based on per-capita income, school enrollment, and life expectancy.

N/A = information not available.

** = less than half the unit indicated.

[a]1998.

[b]1996.

[c]$565 for GDP.

[d]Poverty levels defined as: Armenia (44 percent) $2.15/day and (55 percent) $1/day; Azerbaijan, $4/day; Georgia, $2/day.

[e]Percent of households earning below official average wage.

SOURCES TO TABLE 3.2

Rows 1A and 1B. Azerbaijan: *Azerbaijan Economic Trends,* January–March 2001: percent of GDP (Annex 4.8, p. 153); dollars per capita calculated from budget expenditure in manat (Annex 4.8, p. 152), revalued in dollars at the exchange rate (Annex 2.2, p. 138), and divided by population (Table 3.1 above). Kazakhstan: *Kazakhstan Economic Trends*, January–March 2001: percent of GDP (Annex 4.3, p. 108); dollars per capita calculated from tenge outlays (Annex 4.4, p. 108), revalued in dollars at the exchange rate (p. 8), and divided by population (Table 3.1 above). Turkmenistan: IMF, *Turkmenistan: Recent Economic Developments*, Staff Country Report 99/140, December 1999: percent of GDP (Table 16, p. 106); dollars per capita calculated from budget expenditure in manat (Table 15, p. 105), revalued in dollars at the parallel exchange rate, first half of 1999 (Table 23, p. 113) and divided by population (Table 3.1 above). Uzbekistan: Percent of GDP from IMF, *Republic of Uzbekistan: Recent Economic Developments*, Staff Country Report 00/36, March 2000 (Table 32, p. 69); dollars per capita calculated from budget expenditure in sums, from Ibid. (Table 31, p. 68), revalued in dollars at, alternatively, the official and market exchange rate, from *Uzbek Economic Trends*, January–March 2001 (Table 2.2, p. 35). Other countries: Percent of GDP (except Georgia) from IMF and World Bank, *Armenia, Georgia, Kyrgyz Republic, Moldova and Tajikistan: External and Fiscal Sustainability—Background Paper*, February 6, 2001, Tables 6 (p. 44), 13 (p. 51), 20 (p. 58), and 33 (p. 71); dollars per capita from IMF and World Bank, *Armenia, Georgia, Kyrgyz Republic, Moldova and Tajikistan: External Debt and Fiscal Sustainability*, February 7, 2001, Table 9, p. 28. Percent of GDP for Georgia from *Georgia Economic Trends*, Quarters 3–4, 2000, Table 3.4, p. 19.

Rows 2, 3. Armenia: World Bank and IMF, *Armenia, Georgia . . . Background Paper*, February 6, 2001, Table 7, p. 45. Azerbaijan: *Azerbaijan Economic Trends*, January–March 2001, Table 3.1, p. 39. Georgia: IMF, *Recent Economic Developments and Selected Issues*, Staff Country Paper 00/68, May 2000, p. 4. Kazakhstan: *Kazakhstan Economic Trends*, January–March 2001, Table 3.1, p. 33. Tajikistan: IMF, *Republic of Tajikistan: Statistical Appendix*, Country Report 01/69, May 2001, p. 3.

Row 4. Azerbaijan: *Azerbaijan Economic Trends,* October–December 2000. All other countries: World Bank, World Development Indicators database.

Row 5. Armenia: *Armenia Economic Trends*, October–December 2000, Table 3.3, p. 73. Azerbaijan: *Azerbaijan Economic Trends*, January–March 2001, Graph 3.6, p. 45. Kazakhstan: *Kazakhstan Economic Trends*, January–March 2001, p. 8. Other countries: IMF, *Kyrgyz Republic: Selected Issues and Statistical Appendix*, Staff Country Report 00/131, October 2000, Box 3, p. 29. The figure reported for Turkmenistan in this source is most likely valued at the official exchange rate. It would be much lower at the "curb" rate of exchange. According to IMF, *Turkmenistan: Recent Economic Developments*, p. 11, the average wage in December 1998 was $58 at the official exchange rate and $25 at the "curb" rate.

Row 6. Armenia: The low figure is from IMF and World Bank, *Armenia, Georgia . . . Background Paper*, February 6, 2001, Table 7, p. 45. The higher figure is for 1998, from Republic of Armenia, *Interim Poverty Reduction Strategy Paper*, March 2001, Table 2, p. 20. In 1996 the poverty line was set at a value of the minimum consumption basket of 11,735 drams per month. The average exchange rate then was 413.42 drams/$, which indicates a poverty level of about $0.95 per day. An additional 14 percent of the population was marginally above the poverty line (Ibid., p. 3). Azerbaijan: *Azerbaijan Economic Trends*, January–March 2001, p. 99. Georgia: *Poverty Reduction and Eco-*

nomic Growth Program of Georgia. Intermediary Document, Tbilisi, November 2000, p. 5 (at $2/day). Kyrgyzstan: IMF, *Kyrgyz Republic: Selected Issues and Statistical Appendix*, Table 11, p. 47. According to World Bank and IMF, *Armenia, Georgia . . . Background Paper*, Table 20, p. 58, the poverty ratios were 49 percent at $2.15/day and 84 percent at $4.30/day. Tajikistan: Government of the Republic of Tajikistan, *Interim Poverty Reduction Strategy Paper*, Dushanbe, 2000, p. 2. Turkmenistan: IMF, *Turkmenistan: Recent Economic Developments*, p. 12 (percent of households earning below the official average wage).

Row 7. Armenia: Republic of Armenia, *Interim Poverty Reduction Strategy Paper*, Figure 1, p. 4. Georgia: *Poverty Reduction and Economic Growth Program of Georgia*, p. 5. Kyrgyzstan: The income coefficient is from Kyrgyz Republic National Statistical Committee *(http://stat-gvc.bishkek.su/Eng/Annual/Social.html)*, the consumption coefficient from Kyrgyz Republic, *Interim National Strategy for Poverty Reduction*, 2001–2003, June 13, 2001, Table 2, p. 5.

Row 8. Georgia: *Poverty Reduction and Economic Growth Program of Georgia*, p. 6. Tajikistan: Government of the Republic of Tajikistan, *Interim Poverty Reduction Strategy Paper*, p. 2 (figure for 1997). Other countries: *Azerbaijan Economic Trends*, January–March 2001, p. 98.

much if not most of the industrial structure. Productivity in agriculture was low, and most of the post-Soviet regimes were reluctant to institute radical land reform. The difficulties of casting off the yoke of central planning, inept fiscal-monetary policy that helped bring on high inflation, and inherited health and environmental disasters (e.g., the drying up of the Aral Sea) contributed to the deterioration of economic prospects. Political factors specific to particular countries—such as civil war in Georgia and Tajikistan, or war between Armenia and Azerbaijan and the subsequent blockade of Armenia by Turkey and Azerbaijan—also played an important role. All eight states, in consequence, suffered declines in total output in the early 1990s, with accompanying reductions in living standards. The recessions were sharp and prolonged, except in Uzbekistan.

Official statistics[12] state that only Uzbekistan among the eight has now regained the GDP level of 1991, the last year of the Soviet Union's existence. Comparison of current national income statistics with those of Soviet times is certainly imprecise and potentially misleading, but it is probably indicative that in 2000, six of the eight had GDP levels estimated to be but half (Georgia) to less than four-fifths

[12]Interstate Statistical Committee of the CIS, *Main Macroeconomic Indicators on CIS Countries (www.cisstat.com/mac1_an.htm).*

(Armenia and Kazakhstan) of the 1991 level. (Turkmenistan did not report in this format.) With the exception of Uzbekistan again, the ratios of reattainment of 1991 levels were even lower for agricultural output.

At present only Kazakhstan has reached a gross national per-capita income exceeding $1,000 (Table 3.2). Tajikistan and Kyrgyzstan, the poorest of the eight by this measure, had per-capita incomes about one-quarter as large as Kazakhstan's, but the Armenian and Azerbaijan proportions were not much larger. The middle group of Georgia, Turkmenistan, and Uzbekistan averaged (unweighted) a little over half of the Kazakhstan figure. Kyrgyzstan and Tajikistan were at about the income level of Laos and Uganda; Armenia was comparable to Nicaragua and Georgia to Cameroon.[13]

It is no surprise, after viewing these numbers, to observe that reported average monthly wages range from $10 in Tajikistan to $94 in Kazakhstan. CASC national authorities consider that at least half, and in most cases much more, of the population lives near or below the poverty line, defined in stringent terms. Even in Kazakhstan, 30 percent of the population is found below that line.[14] The burden of poverty is exacerbated by the minimal level of public sector outlays on social services, which are constrained by the small size of the economies and government budgets under continual stress. For that reason, too, the levels of health provision to the population are considerably worse than is indicated by the normalized number of physicians and hospital beds, owing to poor training and shortages of medicines and other supplies.

Poverty also comes tied to considerable inequality of income distribution in the region. The Gini coefficient, where zero measures perfect inequality and one perfect equality, is about 0.25 for the Czech Republic, 0.3 for Poland, and 0.35 for Hungary, whereas it is about 0.4 in Kyrgyzstan, 0.5 in Georgia, and almost 0.6 in Armenia.[15] The prevalence of "informal" or "second economy" features in the region

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[13]"IMF/World Bank, February 7, 2001." Table 8, p. 27.

[14]*RFE/RL Central Asia Report*, 1:23, December 27, 2001.

[15]Republic of Armenia, *Interim Poverty Reduction Strategy Paper*, March 2001, Figure 1, p. 4.

means that in several cases the inequality of consumption is lower than that of income distribution.

High or growing levels of inequality of distribution—or, as noted in the introduction to this chapter, of poverty in general—are neither necessary nor sufficient conditions for political instability. Witness the sharp rise in the Russian Gini coefficient from a 1985 level of about the current Czech figure to 0.48 by 1997, putting Russia in the class of Ecuador, Venezuela, or Nigeria, but without significant threat to the social-political order.[16] A decade of independence has not brought the gains in mass consumption and distributional equity that the CASC leaders promised upon taking power. This failure was surely not lost on the region's inhabitants, and it may well have been a factor in the ethnic-religious tensions that have marked recent years, but it did not visibly shake the political foundations of the national regimes.

Dependence

In 1990 the Soviet republics traded mainly within the Soviet Union; foreign trade involvement as a share of national output was far smaller than a decade later (Table 3.3). In 1999, the CASC states were, except for Uzbekistan, heavily dependent on imports; five of the eight states had import ratios of 50 percent or higher. Export participation in 1999 was generally lower, except in the cases of Kazakhstan, Tajikistan, and Uzbekistan. As developing economies, the eight states generally tend to run substantial trade and current account deficits.

Their trade is highly concentrated in terms of commodity structure (Table 3.4, part 1). Three categories of goods constitute 60 percent or more of exports and imports in seven of the eight countries. It takes only two categories to make up 55 percent or more of total exports by six of the eight states. Azerbaijan presents the extreme degree of concentration among them: petroleum alone accounts for 83 per-

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[16]Cited in William H. Buiter, "From Predation to Accumulation? The Second Transition Decade in Russia," SITE Working Paper No. 156, Stockholm School of Economics, July 2000, p. 7.

cent of exports.[17] All the fuel producers—Kazakhstan, Turkmenistan and Azerbaijan—show heavy concentration, with more than half of total exports derived from fuel. Energy in the form of electric power is also a principal export of Kyrgyzstan and Tajikistan. Each depends heavily in addition on the sale of a single commodity—gold and aluminum, respectively. Uzbekistan appears to have the most balanced structure of the eight.

The degree of concentration is only somewhat less on the import side. As might be expected of developing countries, machinery and equipment is the principal import by six of the eight countries and the third most important by Armenia. Food appears in the lists for five of the eight. Tajikistan's aluminum exports depend heavily on alumina imports.

Table 3.3

Central Asia and South Caucasus: Trade Dependence Ratios, 1990 and 1999
(Exports, Imports and Current Account as Percent of National Output*)

	Exports		Imports		Current Account Balance
	1990	1999	1990	1999	1999
Armenia	16	21	13	50	–17
Azerbaijan	3	34	13	51	–28
Georgia	N/A	27	N/A	46	–8
Kazakhstan	2	43	8	42	–1
Kyrgyzstan	2	43	15	57	–15
Tajikistan	5	68	13	63	6
Turkmenistan	4	42	9	62	–17
Uzbekistan	5	19	10	19	0

*Net material product in 1990 and GDP in 1999; 1990 trade is with non-USSR.

N/A = not available.

SOURCE: 1990 trade from Informatsionno-izdatel'skii tsentr po statistike, *Vneshniaia torgovlia suverennykh respublik i pribaltiiskikh gosudarstv v 1990 godu*, Moscow 1992; net material product from Statisticheskii komitet SNG, *Strany-chleny SNG. Statisticheskii ezhegodnik*, Moscow, 1992. 1999 data: WTO, International Trade Statistics, 2000; World Bank, and Country Briefs (*www.worldbank.org)*.

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[17]In the first nine months of 2001, fuel and energy accounted for over 90 percent of Azerbaijan's exports. *Monitor*, VII:228, December 12, 2001.

Table 3.4

Foreign Trade Concentration in Central Asia and South Caucasus, 2000
Part 1: Commodity Structure

Goods Forming 60 Percent of Exports or Imports (percent of total exports or imports)			
Exports		**Imports**	
Armenia			
Precious stones, metals, and articles	41	Food, animals	25
Base metals	15	Mineral products	21
Machinery, equipment	12	Machinery, equipment	17
Azerbaijan			
Petroleum products	84	Machinery, equipment	40
		Food, animals	19
		Metals and articles	11
Georgia			
Food, vegetable products	29	Machinery, equipment	26
Base metals	24	Food, vegetable products	20
Mineral products	19	Mineral products	19
Kazakhstan			
Fuel, oil products	53	Machinery, equipment	38
Ferrous metals	13	Fuel, oil products	11
		Ferrous metals, products	9
Kyrgyzstan			
Nonferrous metals	47	Machinery	27
Electric power	16	Oil and gas	22
		Food	8
		Light industry products	7
Tajikistan			
Aluminum	50	Electric power	24
Electric power	23	Alumina	21
		Oil and products, natural gas	15
Turkmenistan (1998)			
Oil products, natural gas	55	Machinery, equipment	45
Cotton fiber	22	Industrial materials, excluding chemical and building materials	27
Uzbekistan			
Cotton fiber	31	Machinery, equipment	39
Energy products	12	Chemicals, plastics	15
Metals	8	Food	13

Table 3.4

Foreign Trade Concentration in Central Asia and South Caucasus, 2000
Part 2: Geographic Structure

Exports

	Armenia	Azerbaijan	Georgia	Kazakhstan	Kyrgyzstan[a]	Tajikistan[a]	Turkmenistan[a]	Uzbekistan
CIS	24	14	41	26	40	46	56	36
Russia	15	6	21	20	16	17	7	17
Caucasus	5	4	10	0	N/A	N/A	4	N/A
Central Asia	2[b]	1[b]	N/A	3	23	28	4	3
Others	2	3	10	3	2	1	42	16
Non-CIS	76	86	59	74	60	55	44	35
EU	40	60	21	23	38	36	23	18
Iran	9	**	N/A	N/A	2	2	12	2
Turkey	N/A	6	22	1	1	**	1	3
Others	31	20	16	50	19	17	7	12
U.S.	13	1	2	2	2	**	1	N/A

Imports

	Armenia	Azerbaijan	Georgia	Kazakhstan	Kyrgyzstan[a]	Tajikistan[a]	Turkmenistan[a]	Uzbekistan
CIS	19	32	32	55	43	78	52	35
Russia	15	21	13	49	18	14	7	16
Caucasus	2	1	9	N/A	N/A	N/A	3	N/A
Central Asia	N/A	6[b]	N/A	3	22	55	29	7
Others	2	4	10	3	2	9	13	2
Non-CIS	81	68	68	45	57	22	48	65
EU	34	19	24	20	18	13	26	21
Iran	9	7	N/A	N/A	2	2	4	N/A
Turkey	N/A	10	16	3	4	**	**	9
Others	38	32	28	22	33	7	18	35
U.S.	12	7	10	6	9	**	2	9

[a]1999.
[b]Armenia: exports to Turkmenistan. Azerbaijan: exports to Turkmenistan and imports from Kazakhstan and Turkmenistan.
N/A = information not available.
** = less than half the unit indicated.

SOURCES TO TABLE 3.4

Armenia: *Armenia Economic Trends*, October–December 2000, Table LA3, p. 134 (commodity structure) and January–March 2001, Annexes 6.6 and 6.7, pp. 155–156 (geographic structure).

Azerbaijan: *Azerbaijan Economic Trends*, January–March 2001, Annexes 7.6 and 7.8, pp. 180–181 (commodity) and Annexes 7.10 and 7.12, pp. 183 and 185 (geographic).

Georgia: *Georgian Economic Trends*, Quarters 3–4, 2000, Tables 5.3 and 5.4, pp. 29–30 (commodity) and Tables 5.1 and 5.2, p. 28 (geographic).

Kazakhstan: *Kazakhstan Economic Trends*, January–March 2001, Annexes 7.3 and 7.5, pp. 139, 141 (commodity) and Annexes 7.7 and 7.9, pp. 143, 145 (geographic).

Kyrgyzstan: Kyrgyzstan National Statistics Committee *(http://nsc.bishkek.su/Eng/Database/Index.html)* (commodity); IMF, *Kyrgyz Republic: Selected Issues and Statistical Appendix*, Staff Country Report 00/131, October 2000, Table 44, p. 110, and National Statistical Committee of the Kyrgyz Republic, Direction of Trade Statistics *(http:// nsc.bishkek.su/Eng/Annual/Xc.html and Mc.html)* (geographic).

Tajikistan: IMF, *Republic of Tajikistan: Statistical Appendix*, Country Report 01/69, May 2001, Tables 40 and 41, pp. 44–45 (commodity) and IMF, *Direction of Trade Statistics Yearbook 2000* (geographic).

Turkmenistan: IMF, *Turkmenistan: Recent Economic Developments*, Staff Country Report 99/140, December 1999, Tables 28, 30, pp. 118, 120 (commodity) and IMF, *Direction of Trade Statistics Yearbook 2000* (geographic).

Uzbekistan: *Uzbek Economic Trends*, January–March 2001, Annexes 7.1 and 7.2, pp. 101–102 (commodity: the distributions are calculated net of services, unidentified in this source but labeled as such in previous editions); and Annexes 7.3 and 7.4, pp. 102–103 (geographic).

Armenia is a heavy importer of oil and gas (under "mineral products"); so are Tajikistan and Kazakhstan (because of the latter's huge size and unique energy geography). Indicated Kyrgyz oil imports may be understated: 85 percent of its oil consumption originates abroad but half of all fuel is smuggled into the country.[18] Fuel is not a major import by value for Azerbaijan, but when Russian gas supplies were cut off in October 2000 the deprivation was painful; thousands of Azeris took to the streets in protest.[19]

Part 2 of Table 3.4 shows the relative importance of regional neighbors as well as the outside world in the geographic direction of trade. When the CASC states emerged out of the Soviet Union, they were still largely tied to the Soviet trade network. Over the next decade, however, the direction of trade shifted substantially. Only Turkmenistan now sends more than half its exports to the CIS region, and that is because of gas sales to Ukraine. Nevertheless, Russia is the market for 15–20 percent of the exports by six of the eight countries. The South Caucasus countries do not loom very large as either the export destinations or import sources for both Central Asia and the South Caucasus itself, with a minor exception for Georgia. In two cases, in contrast, Central Asian states are important customers of their immediate neighbors: in order of size of trade share, Kazakhstan and Tajikistan for Kyrgyzstan's exports and Uzbekistan for Tajikistan's.

Extra-CIS states are the destination of 55 percent or more of the exports by six of the eight states of the region. The European Union is now a major customer of the region's exports, its share ranging from 18 percent (Uzbekistan) to 60 percent (Azerbaijan). There are substantial unidentified residuals in the extra-CIS group, but partial breakdowns suggest that most cases involve multiple destinations. Kazakhstan's 50 percent residual consists largely of crude oil sales to offshore locations, particularly Bermuda and the Virgin Islands.[20]

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[18]*Monitor*, VII:151, June 7, 2001.

[19]Ariel Cohen, "The New Tools of Russian Power: Oil and Gas Pipelines," *UPI*, December 29, 2000.

[20]*Kazakhstan Economic Trends*, April–June 2000, Table 9.3, p. 184.

The CIS remains the major source of supply for three of the eight CASC states. Russia provides roughly half of Kazakhstan's imports and 80 percent of the country's purchases from the CIS states. Otherwise, Russia's share ranges from a low of 7 percent in Turkmenistan to a high of 21 percent in Azerbaijan, in a pattern roughly similar to Russia's role in CASC exports. On the import side, three Central Asian countries rely substantially on their Central Asian neighbors: again, in order of size of share, Uzbekistan and Kazakhstan for Tajikistan imports; Uzbekistan for Turkmenistan's; and Kazakhstan and Uzbekistan for Kyrgyzstan's. The South Caucasus states draw most of their imports from extra-CIS sources. Considering how ardently Turkey has sought closer relations with most of the region, its trade is significant only with Georgia. Iran's role is also generally small, again with a single exception—its purchases of Turkmenistan's exports. China is included in the miscellaneous category because of inadequate data.

Russia's supplier role is weightier than indicated in Table 3.4, Part 2, because much of its export to the region consists of fuels, which are vital to the importing economies. This is particularly true for Georgia, which is totally dependent on Russia for natural gas, but Russia is also the main supplier of gas to Armenia. All three South Caucasus states as well as Kyrgyzstan and Tajikistan have experienced temporary cutoffs of oil or gas from Russia or regional partners (Turkmenistan or Uzbekistan). The suppliers usually blamed the consumer states' large arrears of energy debts, but the latter suspected political motives as well.[21]

External economic dependence may occur not only with trade but also with credit. Table 3.5 supplies some indicators of the relative size and burden of external public debt in the region. Kyrgyzstan and Tajikistan carry the largest debt burdens, measured as a percent of GDP, followed by Georgia, Uzbekistan, and Armenia. Calculation of

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[21]See, for example, *Financial Times*, January 4, 2001 (Georgia); *RFE/RL Newsline*, V:18, January 26, 2001 (Kyrgyzstan); *FSU Oil and Gas Monitor*, June 19, 2001, p. 11 (Tajikistan). Kyrgyzstan and Tajikistan in turn have exploited their position as water resource suppliers to exert pressure on Uzbekistan and Kazakhstan. Sadji, "Natural Resources Are Being Used as Political Trump Cards," *Prism* (Jamestown Foundation), VII:5, May 2001, Part 5.

Table 3.5

Central Asia and South Caucasus: Public Sector Debt and Debt Service, 1999

	Debt as percent of			Debt service as % of	
	GDP[a]	Exports	Fiscal revenue	Exports	Fiscal revenue
Armenia	45/30	154[b]	168[b]	16[c]	19[c]
Azerbaijan	21/NA	73	NA	2	3
Georgia	60/56	213[b]	688[b]	13[c]	45[c]
Kazakhstan	24/NA	73	NA	27	NA
Kyrgyzstan	140/94	188[b]	386[b]	24[c]	24[c]
Tajikistan	110/86	128[b]	504[b]	5[c]	20[c]
Turkmenistan	NA	NA	NA	NA	NA
Uzbekistan	23/NA	120	NA	16	NA

NA = not available.

[a]First figure, debt at nominal value; second figure, debt at net present value.

[b]Debt in net present value; includes public enterprise and private nonguaranteed debt for debt/exports but only government and government-guaranteed debt for debt/revenue.

[c]Debt service includes payments on public enterprises and private nonguaranteed debt for export ratios but only government and government-guaranteed debt for revenue ratios.

SOURCES: Azerbaijan: *Azerbaijan Economic Trends*, January–March 2001, Graph 7.13, p. 95. Kazakhstan: *Kazakhstan Economic Trends*, January–March 2001, pp. 70, 72, 137. Uzbekistan: *Uzbek Economic Trends*, October–December 2000, p. 89. The Uzbek debt/GDP ratio is evidently valued at the official exchange rate; the figure would be considerably higher at a weighted average rate, based on Chart 2, p. 102. Other entries from IMF and World Bank, *Armenia, Georgia, Kyrgyz Republic, Moldova, and Tajikistan: External Debt and Fiscal Sustainability*, February 7, 2001, pp. 4, 5, 7, 19.

net present values reduces the ratios because of conditionality features of the loans—particularly, in relative terms, for Armenia and Kyrgyzstan. The debt burden on Georgia, Kyrgyzstan, and Tajikistan appears especially heavy in terms of ratios of exports or budget revenues. Georgia's debt problems may be worse than indicated because exports may be overstated and debt underestimated.[22]

A level of debt service exceeding 25 percent of the value of exports is usually regarded as a threat to financial stability. In extreme cases, as

[22]"IMF/World Bank, February 6, 2001," pp. 5 and 15.

Argentina has demonstrated recently, financial instability can lead to popular disorder. The only country exceeding the 25 percent figure in 1999 was Kazakhstan, but its oil and gas export prospects are so promising, assuming that oil prices remain steady, that the debt/export ratio is likely to decline sharply in the next few years. The same cannot be said for Kyrgyzstan and Georgia; in the latter's case, debt service obligations absorb almost half the government's budget revenues. The Kyrgyzstan situation may have deteriorated further: the republic's finance minister indicated at the end of June 2001 that debt service obligations on the national budget left almost nothing over for socioeconomic purposes.[23]

Table 3.6 looks at the structure of external debt in the four weakest states. Georgia and Tajikistan not only have large public-sector external debts, in absolute value and relative to GDP, but also half or more of the external debt falls to bilateral debt. The CIS region accounts for 36 and 50 percent, respectively, of these two states' totals and, therefore, the lion's share of their bilateral components.

Table 3.6

Public-Sector External Debt of Four CASC States, End 1999

	Armenia	Georgia	Kyrgyzstan	Tajikistan
Total government and gov't-guaranteed debt, million $	854	1,678	1,383	887
Structure in percent of total				
Multilateral	75	50	68	36
Bilateral	21	50	32	60
Russia	13	11	12	32
Other FSU	14	25	1	18
Commercial and guaranteed	4	0	0	5

SOURCE: IMF and World Bank, *Armenia, Georgia, Kyrgyz Republic, Moldova, and Tajikistan: External Debt and Fiscal Sustainability,* February 7, 2001, Table 1, p. 6.

[23]*RFE/RL Newsline*, V:125, July 2, 2001. The minister reported that the government's foreign debt on January 1, 2000, was $1.76 billion, notably higher than the figure shown in Table 3.6, and reached $2 billion as of the date of his report, one-third greater than GDP. *FSU Oil and Gas Monitor*, April 10, 2001, p. 7; *RFE/RL Newsline*, V:137, July 23, 2001; *RFE/RL Newsline*, V:239, December 19, 2001.

Russia is a particularly large creditor of Tajikistan, but it is also the source of 11–13 percent of the total government and government-guaranteed debt in the other three states.

Concentration of trade joined to debt dependence makes a potentially dangerous combination. Armenia, for example, has struggled to cope with its debts for Russian natural gas and nuclear fuel. In a debt-equity swap, the Russian gas suppliers Gazprom and Itera together acquired 55 percent of the Armenian gas distribution monopoly Amrosgazprom. In the second half of 2001, Moscow was negotiating for a stake in various Armenian state-owned enterprises, in return for writing off Yerevan's remaining $88 million debt.[24] It has been reported that Moscow offered deep discounts on future gas supplies if Armenia joined the Eurasian Economic Community (consisting of Russia, Belarus, Kazakhstan, Kyrgyzstan, and Tajikistan).[25]

Armenia is not the sole case in point. The agenda of the September 2001 session of the Kyrgyzstan-Russia Intergovernment Committee on Trade and Cooperation included the transfer to Russia of shares in 27 domestic industrial enterprises in partial repayment of Kyrgyzstan's $150 million debt to Moscow.[26] The leadership expressed strong interest in having Russian companies buy into Kyrgyz businesses, evidently due to the apparent failure of Kyrgyzstan's privatization effort in enlisting Western participation.[27] In any case, the political-economic implications of a substantial Russian stake in Kyrgyzstan's economy remain the same. Economic subordination to a regional hegemon, if that is what results from such negotiations, is of course not equivalent to political destabilization. The implicit conflict with national goals and interests, however, can intensify internal political discontents.

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[24] *FSU Oil and Gas Monitor*, April 10, 2001, p. 7; *RFE/RL Newsline*, V:137, July 23, 2001; *RFE/RL Newsline*, V:239, December 19, 2001.

[25] *Russia's Week (*Jamestown Foundation), VI:935, September 26, 2001.

[26] *RFE/RL Newsline*, V:173, September 12, 2001.

[27] *Interfax Daily News Bulletin*, November 11, 2001. See also *RFE/RL Central Asia Report*, 1:17, November 15, 2001.

PROSPECTS

The solutions to the economic problems posed by CASC poverty and external dependence ultimately reside in structural reform and economic growth. Reform is likely to be a necessary condition for sustained growth and a co-determinant of success in reducing poverty significantly. Stepping up the rate of growth, in turn, would contribute to poverty reduction directly, by increases in employment and incomes, as well as indirectly, by augmenting the resources available for poverty reduction. Growth could help ease the burden of debt by increasing government revenues and perhaps also by boosting exports, but enlarging the government's revenue base is also the task of fiscal reform. The content of the required reforms, in addition to fiscal changes, is well known. It includes (in no particular order) reducing public-sector corruption; further privatization, but to profit-seeking entrepreneurs rather than would-be asset strippers; strengthening the rule of law in all spheres of the society; instituting or extending nondiscriminatory regulatory regimes; creating a modern banking system; repairing the social safety net by restructuring the social services; land reform; eliminating disguised unemployment, which distorts labor resource allocation; and so on. The seriousness with which the CASC states prosecute reform programs, however, remains to be seen; the record of the 1990s was disappointing in most cases.

All eight states recorded economic growth in 2000 and 2001, but this period of progress is too brief, against the background of sustained misadventure in the 1900s, to warrant unconstrained optimism. The eight states appear to fall into two groups in terms of their current growth prospects, the three major energy producers and exporters in one category and the other five states in a second. Azerbaijan, Kazakhstan, and Turkmenistan have large oil and gas deposits, which have attracted the interest of the major international conglomerates. (Uzbekistan has large gas reserves but has not yet become a significant energy exporter.) Because of the region's isolation from world markets, distribution—essentially, via pipelines—has been more of a problem than production. It is likely, however, that the pipeline problems will be resolved in one fashion or another, if oil and gas prices remain in roughly the current range.[28] In that case, energy exports should become an increasingly important driver of the three states' economic growth. By the same token, their debt management burdens, which are already relatively low, should be further reduced. On the other hand, the introduction to this chapter pointed to a number of potential downsides of energy concentration, apart from market price fluctuation: failure to channel oil and gas proceeds into productive investment, tenuous links between primary product extraction and development of manufacturing and services, "Dutch disease," and vulnerability to external pressure. As already noted, the energy producers are aware of these difficulties and hope to be able to sidestep them.

The growth prospects of the other five states will be conditioned in part by the character of the external environment. Russia's relative weight in the CASC's trade and debt is not what it was in the early and middle 1990s, but the Russian financial crisis of August 1998 hurt several of the region's economies badly, if temporarily. Another sharp reduction in Russian demand, especially if accompanied again by steep devaluation, would naturally be damaging. It seems less likely at this time because of the improvement in Russia's growth prospects and macroeconomic management. In general, however, the high trade participation ratios shown in Table 3.3 indicate that external trade shocks, whether coming from Russia, the European Union, or other significant partners, could set back growth substantially in the second group of CASC states. Finally, reluctance of lenders to reschedule debt on favorable terms or insistence on hardening of credit terms for new debt would also constitute a form of external shock.

Domestic policy and action are, however, fundamental for the group of five. Four of them—Uzbekistan is the exception—have specific poverty-reduction programs, worked out in the context of IMF/World Bank lending programs, with targets for increasing income levels of the poor, decreasing infant and child mortality, raising education and health standards and service, and the like. Whether these programs will succeed to any extent will depend in part on success in

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[28]For more detail and a somewhat different point of view, see Chapter Five of this report.

fiscal-monetary policy—increasing budget revenues, decreasing deficits, and controlling the money supply. More important perhaps is increasing investment in the economy, particularly by attracting foreign investment, which in turn depends on transforming the domestic business climate through the structural reforms noted earlier. The IMF and World Bank believe that Georgia, Kyrgyzstan, and Tajikistan face difficult situations of balance of payments and debt over the current decade, even under a relatively benign scenario of internal macroeconomic adjustment and reform coupled with a shockless external environment. An alternative scenario with less favorable internal and external conditions yields near-crisis conditions. Armenia's debt sustainability problem seems manageable.[29] Uzbekistan's situation is obscured by doubts about the reliability of government statistics.[30] Persistent government refusal to liberalize its foreign exchange and trade regimes, which has only recently begun to yield to international pressure, raises additional questions about Uzbekistan's near- and mid-term prospects.

All forecasting for the CASC economies, however, will now have to be examined in the light of a potentially cardinal transformation of the regional environment: the U.S. government's war against terrorism triggered by the events of September 11, 2001. Heightened U.S./ allied presence in the wake of military action that was supported to varying degree by all eight states—but especially by Kyrgyzstan, Tajikistan, and Uzbekistan—will surely have an impact on the region. The potential economic effects of sustained foreign presence may be of various kinds:

- When the U.S. military campaign began, it was feared that perhaps hundreds of thousands of Afghan refugees would flee to the neighboring Central Asian states and disrupt their economies. That concern has abated with the defeat of the Taliban–Al Qaeda regime, but tribal-ethnic conflict may yet erupt in dimensions that could resurrect the specter of large-scale refugee movements.

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[29]"IMF/World Bank, February 6, 2001," and "IMF/World Bank, February 7, 2001," along with an additional companion paper.

[30]IMF, *Republic of Uzbekistan: Recent Economic Developments*, Staff Country Report 00/36, March 2000, p. 7.

- In recent years, Central Asia in particular has experienced a major influx of drugs, mainly enroute from south Asia to Russia and Europe but also increasingly distributed to the Central Asian populations. The danger of widespread drug addiction was exacerbated by an incipient AIDS epidemic, a combination that threatened to play havoc with the regional economies and seriously disrupt their political-social order. Coalition military action may have disrupted Taliban drug flows, but they may be replaced by production in Afghanistan, still far from centralized control by the new Kabul government, or in parts of Central Asia. Presumably, replacement of drug flows would be accompanied by a reorganization of distribution networks. As the drug trade is intertwined with local criminal networks and depends on the corruption of government officials, such reorganization could upset political balances and lead to a refashioned struggle for power.
- Depending on the scale, character, and duration of the U.S./allied presence, significant foreign exchange injections into the national economies could stimulate economic growth and employment. It could also, however, accelerate local currency price inflation, increase the inequality of income distribution, and perhaps even intensify economic crime and corruption. War tends to stimulate capital flight and inhibit the inflow of foreign investment, but extensive military action in Afghanistan has been brief. Restoration of military security in the region, even without substantial political reform, joined with augmented foreign exchange resources for the national governments, could stimulate external credits and the inflow of foreign investment.
- Military conflict does not ordinarily promote trade. Kyrgyzstan and Tajikistan depend heavily on trade with other Central Asian states and could be hard hit if significant hostilities resumed. Realization of the promise of security stabilization in the region, in contrast, would probably stimulate intra- and extraregional trade.
- Caspian basin energy development may also be affected. With military action confined to Afghanistan and its neighborhood, oil and gas pipeline construction in the Caspian–Black Sea area should be able to proceed unhindered, particularly if energy prices stabilize. The dream of piping gas from Kazakhstan and

Turkmenistan through Afghanistan to Pakistan, India, and, via the Arabian Sea, to East Asia may be revived. But if disturbances spread westward, possibly even to the Persian Gulf, the shock to energy development could be severe.

- An interesting question concerns the political economics of CASC interstate relations. For example, Uzbekistan's currently central role in supporting the coalition might strengthen its economic as well as political leverage over its weaker neighbors. The principal issue, however, is the future role of Russia in the region. Before September 11, three of the five Central Asian states (Kazakhstan, Kyrgyzstan, and Tajikistan) had joined Russia and Belarus in a customs union, which was raised in status to the Eurasian Economic Community. The economic and political integration of the CIS is a Russian government goal that antedated the accession of Vladimir Putin, but he energized what appeared to be a moribund policy. In the past, CIS integration was retarded and distorted by the clash of interests of the participants, especially by the opposition of the smaller states to what they perceived as Russia's hegemonic ambitions. Such a conflict characterizes much of the history of Caspian oil and gas development over the last seven or eight years.[31]
- Resistance by the smaller CIS states to Moscow's integrationist ambitions was made possible by Russian economic and military weakness. Recent strengthening of the Russian economy has raised the possibility of a reversal of the power balance. Uzbekistan's President Karimov noted that "present-day Russia is not the Russia of the 1990s." He warned that "if the ruble and Russian economy strengthen, none of us will be able to escape its influence."[32]
- If the members of the Eurasian Economic Community are serious about implementing their unity promises, they will be opting for one form of economic integration against an alternative, with

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[31]On Russian policy regarding integration of the CIS, see Abraham S. Becker, "Russia and Economic Integration in the CIS," *Survival*, XXXVIII:4, Winter 1996–97, pp. 117–136. On the Caspian oil and gas conflict, see Becker, "Russia and Caspian Oil: Moscow Loses Control," *Post-Soviet Affairs*, XVI:2, 2000, pp. 91–132.

[32]Cited by Igor Torbakov, "Economic Clout Gives Russia Growing Power in CIS," *Eurasia Insight*, December 6, 2001 *(www.eurasianet.org)*.

the increasingly globalized world market and especially with Europe. It is difficult to believe that such a choice would not have major consequences for the economic growth and welfare of these economies. The most important Central Asian member of the community, Kazakhstan, evidently seeks a Janus-like position. On a visit to President Bush in Washington, Kazakh President Nazarbayev and his host proclaimed a "long-term strategic partnership and cooperation" between the two states and stressed the need to integrate a prosperous, democratic Kazakhstan into the global economy.[33] At the same time, Nazarbayev is CASC's most consistent and enthusiastic supporter of CIS economic integration and the Eurasian Economic Community in particular. Riding two horses heading in different directions seems, however, inherently unsustainable.

- Russia exhibits signs of uneasiness about the prospect of long-term American presence in Central Asia. This is partly evoked by such statements as U.S. Secretary of State Colin Powell's declaration that the American "interest in the region should be permanent and these relations will continue after the [Afghan] crisis," or President Bush's promise to seek "long-term partnership" with Uzbekistan.[34] One visible Russian reaction is to bolster its military position in the region. The CIS summit meeting in Moscow on November 30, 2001, called for closer cooperation between CIS security organs to strengthen the new CIS counterterrorist center. The center was viewed as a step toward the creation of "a global system to counteract terrorism in close coordination with all interested nations and organizations, and with the United Nations (UN) and Security Council playing the leading role."[35] Russia is now seeking permanent military facilities for its forces deployed in Tajikistan.[36]
- In sum, Russian political-military pressure on Central Asia—perhaps on the South Caucasus too—to prevent the solidification of

[33] *RFE/RL Central Asia Report*, 1:23, December 27, 2001.

[34] *RFE/RL Central Asia Report*, 1:21, December 13, 2001.

[35] *RFE/RL Central Asia Report*, 1:20, December 6, 2001.

[36] *RFE/RL Newsline*, V:232, December 10, 2001; *RFE/RL Central Asia Report*, 1:21, December 13, 2001.

a long-term U.S. presence, along with a possible clash of political-economic interests over integration in the CIS and the Eurasian Economic Community, are also potential threats to regional stability.

These considerations of the possible implications of the Afghanistan war and its aftermath point in different directions, toward economic progress and political stabilization or toward conflict and destabilization. It was noted at the beginning of this chapter that generalizations about the connection between economic factors and political stability are problematic and controversial. The difficulties loom larger in a period of rapid change in the external environment, as is now the case in the CASC. Whether we will indeed see a substantial, long-term U.S./allied presence in the region and, if so, what character it will take are very much open questions at present. So too therefore are the possible consequences for the CASC countries. They may become clearer over the next year or two as the direction of U.S. policy and the reactions of regional actors unfold.