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# Economic Dimensions of Security in Central Asia

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# Summary

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## Objective

This report assesses the political implications of economic and related social problems in the five post-Soviet Central Asian states of Kazakhstan, Kyrgyzstan, Tajikistan, Turkmenistan, and Uzbekistan. It also suggests U.S. policy measures that would help address these problems, consistent with broader U.S. goals in the region. The September 11, 2001, attacks on the United States led those in policy-making circles to realize that instability, failed and failing states, and economic and political underdevelopment present security concerns not just to the states that suffer directly from these problems but to the global community as a whole. From this perspective, political, social, and economic trends in Central Asia merit attention.

## The Implications of Economic and Social Problems for Stability

Economic development will play a pivotal role in the social and political evolution of post-Soviet Central Asia. Despite the promise of abundant natural resources and increased international attention in the wake of Operation Enduring Freedom, the people of Central Asia face an uncertain future. U.S. policymakers are increasingly acknowledging that the security challenges in the region may well include the

effects of widespread dissatisfaction with economic policies and corruption, the growth of organized crime networks, and deteriorating social conditions. The relationship between economic policies and political developments in Central Asia is not straightforward. However, the record suggests that a lack of economic opportunities can play a major role in fostering instability and, potentially, conflict, particularly when it is compounded by perceptions of government mismanagement and political disenfranchisement. As the United States defines its policies toward the states of Central Asia, it must view economic development in the region as itself a long-term security concern. Popular discontent in Kyrgyzstan and Uzbekistan in early 2005 underscore these issues and their importance.

Uzbekistan, the most populous and geographically central state in Central Asia, has emerged as the central player in the prospects for regional development and long-term economic growth. Uzbekistan is facing a transition period where policy choices regarding economic and political liberalization directly affect its ability to alleviate the discontent associated with poverty and unemployment. These choices will have implications outside Uzbekistan and could further contribute to the division of Central Asia into a relatively wealthy Kazakhstan and a poor, fractious, southern flank.

### **Economic Trends**

From an economic perspective, the states of Central Asia may be characterized as much by their differences as by their similarities.

After a difficult market transition period in the early 1990s, Kazakhstan has posted impressive economic growth figures in recent years, largely as a result of its relatively favorable geographic position, billions of dollars of foreign direct investment (FDI) in its oil and gas sectors, and liberal economic policies. Kazakhstan has accounted for almost 50 percent of the region's total gross domestic product (GDP) and 85 percent of cumulative FDI since independence and is more closely linked with Russia in terms of infrastructure and trade than with the rest of Central Asia. (See pp. 7–8.)

Uzbekistan and Turkmenistan, both endowed with substantial natural resources, have failed to implement any significant political

and economic reform measures. Despite their economic potential, they have attracted the lowest FDI in the region, relative to the size of their economies, because of major state interventions in their economies and an unfavorable investment climate. Turkmenistan, a major natural gas producer, will likely remain an isolated, command economy, linked to the rest of the region primarily through natural gas trade. The prospects for Uzbekistan's long-term economic growth and stability remain uncertain and will depend on the regime's approach to balancing internal security challenges and political and economic liberalization. (See p. 8.)

Tajikistan and Kyrgyzstan, the smallest economies of the region, remain highly dependent on foreign assistance and an undiversified trade structure, which has made them highly sensitive to fluctuations in commodity prices. However, both have a relatively favorable track record with international donors, who are actively involved in infrastructure projects and debt restructuring, which will free up money for greater investment spending. (See p. 8.)

### **Sectoral Trends**

The Caspian Sea region promises to become an important second-tier supplier of oil to the world market and a major regional supplier of natural gas over the next several decades. Hydrocarbon exports will be a critical source of government revenues in Kazakhstan and Turkmenistan. On balance, the existence of significant hydrocarbon and mineral reserves gives Kazakhstan and Turkmenistan an opportunity to bolster their geopolitical relevance and economic development. Although they are only in the early stages of their post-Soviet hydrocarbon boom, Kazakhstan, Turkmenistan, and Uzbekistan already suffer from some of the classic institutional pathologies evident in other resource-rich regimes, such as off-budget petroleum (and other mineral) accounts, and oil and gas ministries that wield disproportionate influence over other elements of the government. (See pp. 36–47.)

However, the prospects for foreign direct investment outside the energy and mining industries are bleak, largely because of an unfavorable and, in most cases, corrupt business environment, but also

because of decaying infrastructure and the remote, landlocked geographic position of the resources.

Poverty is disproportionately severe in the countryside, and the agricultural sector is the chief employer of the rural populations of Central Asia. However, agricultural productivity is constrained by major state intervention in both the input and output markets and by severe water shortages, particularly in the cotton and grain-growing areas in Uzbekistan and Turkmenistan. Severe unemployment has led to a northerly seasonal migration from all the Central Asian states to Russia and Kazakhstan. Tajikistan grows less than one-half of its food needs and remains dependent on food aid and imports from abroad. The lack of arable land and farm credit for crops other than cotton has discouraged private investment in other agricultural commodities in Tajikistan and malnourishment will remain a challenge there.

Water is a key security issue, particularly for Turkmenistan and Uzbekistan, which have a high demand for irrigation water to support their over-leveraged agricultural industries. Although there is little prospect for a multilateral solution to water allocation in the region, the prospects for a “water war” are slim. Most conflicts over water have been local, with little or no ethnic dimension. (See pp. 29–36.)

### **Social Trends**

Economic development depends on a healthy, well-educated, and capable workforce. The deterioration of the health care system in Central Asia has cast doubt on the ability of the region to confront some of the new health care challenges it faces, such as HIV/AIDS. Although Central Asia still enjoys a high level of literacy for its level of income, the steady deterioration of the educational system over the past decade has increased the mismatch between the skill sets of young Central Asians and those demanded by the global market, potentially retarding long-term economic growth. This is especially severe in Turkmenistan, where educational standards have deteriorated significantly in recent years. (See pp. 52–54.)

Trade in illicit drugs has empowered organized crime networks and negatively affected the health and personal security of citizens in

Central Asia. There has been a discernible shift in drug trafficking of Afghan opium from traditional Iranian routes toward Central Asia in recent years. The introduction of heroin use by intravenous injection has increased the spread of HIV/AIDS in the region, which threatens to become a public health crisis in the future. The nature and scope of the organized crime networks and their possible connections, in some cases, with the regimes in Central Asia are very difficult to measure. (See pp. 49–52, 54–59.)

### **Foreign Assistance In Central Asia**

The prevailing wisdom since the collapse of the Soviet Union has been that the presence of Western political and economic entities would have a beneficial effect on democratization and economic reform. However, the record of international financial institutions, multinational corporations, and international nongovernmental organizations has been decidedly mixed in Central Asia, and particularly discouraging in Uzbekistan and Turkmenistan. (See pp. 61–70.)

If one goal of international assistance is to help a country eventually access the international private capital market, Kazakhstan can be regarded as a success. Today, Kazakhstan has access to international financial markets, enjoys fairly well developed domestic financial markets and institutions, and has posted impressive economic growth figures over the past several years. Donors have helped Kyrgyzstan and Tajikistan avert possible humanitarian crises and, some would argue, implement preliminary democratic and market reforms. However, both are expected to remain highly dependent on foreign aid and a very limited slate of export commodities. The international community has had very little success in promoting economic or political reform in Uzbekistan and Turkmenistan and may, in fact, have inadvertently delayed it by lending to them in the 1990s.

## U.S. Policy Options

The United States must balance its strategic military relationships in the region with the potentially disparate goal of fostering domestic reform and sustainable economic development. Economic development will be crucial to long-term development in Central Asia and broader U.S. interests in the region. However, it is unclear whether these states have the institutional capacity to implement sound and lasting economic policies and whether the United States and the international community are offering the appropriate combination of incentives to enable this. One challenge for the United States and the international community is to offer sound policies despite the opaqueness of the internal dynamics of the region's regimes, particularly in Uzbekistan and Turkmenistan. As the United States clarifies its long-term military relationships and commitments, it should consider the region's economic development as a long-term security concern itself. (See pp. 71–73.)

Several issues merit attention in the discussion of economic dimensions of security in Central Asia:

- Central Asia will increasingly diversify its economic and military relationships with neighbors such as Russia, China, and Iran, potentially crowding out U.S. influence in the region. The United States does not have a direct, compelling economic interest in Central Asia outside Kazakhstan's oil sector. Nor does most of Central Asia depend on direct economic assistance from or trade with the United States. Thus, Central Asia's economic future lies primarily within its own neighborhood. However, U.S. actions may have an effect on shaping the involvement of Central Asia's neighbors in the region. Insofar as the other regional powers share the U.S. goals of fostering development in the region, they should be engaged. In particular, cooperation with Russia may be crucial.
- Regime change in the region may occur with little warning and in spite of the efforts of the United States. If U.S. policymakers decide to maintain a military presence there, it may be necessary

to consider a wider range of approaches that lower the risk of long-term denial of access and perceptions of the United States as a regime patron. Although some have argued that a U.S. military presence could be used as a vehicle for encouraging domestic reform, the record to date provides little grounds for optimism. At a minimum, a lower-profile presence and hedging strategies should be part of U.S. strategic planning.

- A “nuanced” approach may be necessary in dealing with the more authoritarian regimes in Central Asia. The reality of governance in the region is that domestic policies are often the outcome of complex interactions among the elite stakeholders within the regime rather than of a centralized decision process. Although human-rights concerns may test the U.S. goal of promoting foreign policy at the intersection of our “vital interest and deepest beliefs,” disengagement from Central Asia may compromise U.S. ability to attain overarching goals in the region. Policymakers should consider the costs and benefits of engaging alternative power centers within and outside of these regimes, possibly enlisting the support of other regional powers where common ground can be found.
- Economic and military assistance to the region should be more sharply focused to avoid the highest risk outcomes. In particular, failed state scenarios for Uzbekistan would result in major regional problems that would undermine broader U.S. goals, such as counterterror and counternarcotics strategies. However, policies that may be critical to stability, such as agricultural reform and free trade, remain important domestic political decisions and thus beyond the direct influence of the United States or multilateral institutions. Although a portfolio approach to assistance in the region has merit, a greater focus of diplomatic capital and economic resources on specific issues, such as political liberalization, may be necessary.

In conclusion, economic development will be crucial to the future of Central Asia and broader U.S. interests in the region. Although there are indications that the states of the region recognize

this, it is unclear whether they have the institutional capacity to implement sound and lasting economic policies and whether the United States and the international community are offering the appropriate combination of incentives to enable this. The United States has limited ability or interest in becoming a regime patron but still may play a significant role in shaping the prospects for development in the region by influencing the nature and pace of political and economic reform, realizing that the principles and interests behind U.S. involvement are more enduring than any single regime is likely to be.