

THE ASPECTS OF CENTRAL ASIAN ECONOMIC INTEGRATION AFTER 1991:  
THE REASONS OF INEFFICIENCY

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## **ABSTRACT**

### **THE ASPECTS OF CENTRAL ASIAN ECONOMIC INTEGRATION AFTER 1991: THE REASONS OF INEFFICIENCY**

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This study seeks to analyze the dimensions of economic integration in the Central Asia after the independence. The collapse of the Soviet Union opened new perspectives for Central Asian states and gave chance to follow national policies independently. However, used to be parts of the big economic complex of the former Soviet Union and being lack of government experience in public and private economy made them to cooperate with old and new markets. The study argues that although there were established numbers of economic integration or cooperation institutions none of them could meet the region's economic expectations and needs. They were just results of unstable economic, political and social transition policies. Therefore well-functioning economy oriented cooperation institutions have not been established during the transition period due to different reasons. Analyzing of these reasons is the main goal of thesis. This study also argues that transition period put Central Asian states into the complexity of choices; economic interdependence or socio-political independence. Pushing forward previous choice offers lowering barriers to regional trade and transit, and to mobility of capital and knowledge and, to access to world market. Whereas, political and social development in national level does not suits previous one.

**Keywords:** Central Asia, Integration, Cooperation, Transition Economies, Regional Organizations

## ÖZ

### 1991 SONRASI ORTA ASYA ÜLKELERİ ARASI EKONOMİK İŞBİRLİĞİ GİRİŞİMERİ: BAŞARISIZLIK NEDENLERİ

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Bu çalışma, bağımsızlık sonrası Orta Asya bölgesindeki ülkeler arası ekonomik işbirliği girişimlerini incelemektedir. Sovyetler Birliğinin çökmesi Orta Asya ülkelerine birbirinden bağımsız karar alma ve hareket etme olanağı sağlamıştır. Ancak, Orta Asya ülkelerin daha önceden merkezi yönetimin birer parçaları olması ve gerek kamu, gerek ise özel alanlarda deneyim yetersizliği, bu ülkeleri ekonomik anlamda eski işbirliğini devam ettirmeye ve yeni piyasalarla işbirliğine gitmeye yönlendirmiştir. Çalışmanın amacı Orta Asyada ki ekonomik işbirliği amaçlayan kurumları ve bu kurumların kapsam alanlarını, gelişme basamaklarını kapsamaktadır. Bu çalışmada bölgede faaliyette bulunup da bekleneni karşılayamayan ekonomik işbirliği amaçlayan bu kurumların başarısızlık nedenleri incelenmeye çalışılacaktır. Geçiş dönemi politik bağımsızlık ve ekonomik işbirliği ikilemiyle karşı karşıya kalan Orta Asya ülkelerindeki durum ele alınacaktır.

Anahtar Kelimeler: Orta Asya, Entegrasyon, Ekonomik Birleşmeler, Geçiş Ekonomiler, Bölgesel Örgütler, Uluslararası Örgütler

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To my mother,  
Manasova Masuda (1950-2004),  
always trusted in me.  
Апама арналат,  
Манасова Масуда (1950-2004),  
Ар бир кадамым сиздин ишенчинизе...

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## LIST OF ABBREVIATIONS

### ABBREVIATIONS

<b>CACO</b>	Central Asian Cooperation Organization
<b>CAU</b>	Central Asian Union
<b>CAEC</b>	Central Asian Economic Community
<b>CAREC</b>	Central Asian Regional Economic Cooperation
<b>CIS</b>	Commonwealth of Independent States
<b>GUAAM</b>	Georgia, Ukraine, Uzbekistan, Azerbaijan, Moldova
<b>ECO</b>	Economic Organization Cooperation
<b>ECOTA</b>	Economic Organization Cooperation Trade Agreement
<b>EEC</b>	Eurasian Economic Community
<b>EU</b>	European Union
<b>NAFTA</b>	North American Free Trade Agreement
<b>RCD</b>	Regional Cooperation for Development
<b>SCO</b>	Shanghai Cooperation Organization
<b>SPECA</b>	Special Program for the Economies of Central Asia
<b>SSR</b>	Soviet Socialist Republic
<b>SU</b>	Soviet Union
<b>TRACECA</b>	Transport from Europe to Asia through the Caucasus and Central Asia
<b>UN</b>	United Nations
<b>USSR</b>	Union of Soviet Socialist Republic

# CHAPTER 1

## Introduction

As the process of economic globalization continues in the world, there is a trend towards regional economic integration. Economic integration and cooperation efforts have existed in various parts of the world, but it has never risen as rapidly as it had in after the dissolution of Soviet Union. Presently, practically all countries are members of at least one organization. It is therefore important to understand that why countries have resorted to economic integration, and examine the various aspects and forms of economic integration in particular regions, and assess their roles in advancing economic integration. By eliminating the barriers to trade between the participant countries, regional economic integration encourages the development of the regional economy and trade, which helps to enhance social welfare.

With the collapse of the Soviet Union Central Asian states' national economies have suffered due to breakdown in traditional market structures and a lack of alternative trade. Therefore, to solve Soviet type economic interdependency among the republics and the infrastructure set in accordance with this model were immediately on the agenda of Central Asian states after the independence. Additionally, lack of experience in regulation, both in the public and private sectors made the situation more complex. The choices were more complex than it seemed. They must not only decide whether to cooperate and integrate but also with whom to cooperate and integrate and how deeply to cooperate, because the political, social and economic cost of each integration will affect the structure of states, which had just entered triple transition period. Furthermore, benefits of integration they will join in vary with size of market and level of development. In other words these states faced with dilemmas of choice generated by the economic and political costs and benefits of reintegration with different states, and the resulting attempts to create new forms of economic cooperation.

Central Asian countries are in the process of transition from centralized economy to market economy. They have been trying to set up ties with other parts of world. In this respect, within the short period of time they established diplomatic

relations with most countries of the world, became members of the United Nations and international organizations, signed hundreds of interstate treaties and trade agreements, and entered into highly complex trade and economic relations with over 140 countries (Gleason, 2001). However, during the transition period interstate economic relations in the Central Asia have remained very complicated. It seems to be like that the economic relations of these states have developed under the simultaneous influence of two opposite directions; integration and disintegration.

As it has analyzed in studies focused on these issues it is difficult to find right answer to that why the Central Asian states need to integrate or cooperate. Some of scholars support the integration in the region due to internal factors, some of them found themselves in opposite side underlying external factors. It seems that this issue is open to discussion, since the factors affecting the economic integration in the region have been changing within time. In addition, according to some scholars Central Asian states could not be successful by themselves due to lack of experience and financial resources (Rumer, 1999). They should take part in some outside integration organizations. In order to overcome sharp economic decline Central Asian states did not only cooperate with former Soviet republics but also other regional actors such as China, Iran and Turkey.

According to Tang (2001) thanks to economic policies of the long Soviet Era that were designed to create interdependence among Soviet Republics, Central Asian countries have remained politically and economically dependent on Russia. Moreover, Russia as well deeply interconnected with the region. Thus the economic integration or cooperation of region was generally shaped by Russia, because, economic instability in these states can lead to a serious security problem that Russia would not able to control. From the security and political perspectives Russia has to be concerned over the region. Additionally, there is millions of ethnic Russian in the region. All of these factors made Russia to coordinate Central Asian economies and their cooperation.

However, to Primbetov (2006), and Asymbekov (2006) economic integration was result of sharp and unexpected economic decline in the region not the result of Russia's concern. Linked together by economic relations, infrastructure

communications and social policy, the Central Asian republics after the independence were badly in need of former relations. Otherwise, no sector of their economy could function properly. They found themselves in a state of total socioeconomic decline. In addition, the common infrastructure could not be destroyed right away. Therefore, economic cooperation was inevitable. For them, gaining political independence and facing with similar problems Central Asian new sovereign states fell into more serious economic dependence.

Another factor that made Central Asian economies to integrate was the specialization over the particular fields of economy. As a result of centralized economy Central Asian Uzbekistan was typically associated with cotton and gold, Turkmenistan with cotton and natural gas, Tajikistan with cotton, electricity and aluminum, Kyrgyzstan with gold and electricity while Kazakhstan was largely identified with oil and raw material, and grain. The common structure and specialization over particular field made them to cooperate their economies. However, with respect to Bohr's approach this made their economy more competing than complementary (Bohr, 2004).

In the literature, these states are regarded as a homogenous not only due to economic interdependence or common economic structure but also due to shared social characteristics (Akiner, 1998). Sharing common Turkic culture, language and religion they handled as a significant part of Turkic world. They accepted as one region with respect to social values and historical background.

International organizations were another encouraging factor of integration into one single regional economy. They argued that the economies of the Central Asian states, taken separately, were too small and weak for the foreign investors. They could attract foreign investment only by uniting their markets and creating larger economic spaces. In addition, international financial and donor organizations stressed that training programs and other forms of technical assistance would be provided and they would be effective if a regional single market approach was applied (Asymbekov, 2006).

Around the Central Asian economic integration not all of scholars have same approaches, however. As Rumer (2000) has noted, the Central Asian states lack of



objective preconditions for regional unity. For him they, have neither a shared interest in a single market, as in the European Union, nor large investment resources from one of the member states, as in the North American Free Trade Agreement. He argued that trade intensity in the Central Asia is a relatively low and external trade dependence is high, export consists mainly of agriculture and raw materials. Moreover, informal small sized trade played more significant role than formal trade among the states and there is large difference among the Central Asian states' market system.

There are many studies in the literature discussed over the arguments supported weak and strong sides of Central Asian economic integration (Gleason, 2003., Rumer, 1999, Primbetov, 2006., Pomfret, 2006). Within the one and half decade these discussions and unsatisfactory efficiency of inter-state cooperation have raised both theoretical and practical questions. What are the principal dimensions of economic cooperation or integration in Central Asia? Whether these integration based institutions reflects any theoretical approaches or not? Were they efficient or not, if not what are the reasons? Are there any new perspectives of integration? In this study the answers of these questions would be tried to be argued. While the main research question of the study is that could Central Asian states integrate economically? To analyze the questions, the social factors and common historical background of the region would be taken into consideration. Since, at the beginning of independence there was general thought that the integration of Central Asia would be easier and stronger than other regional integrations since they have been sharing common culture and social and economic values. However, on the contrary of general opinions it worked opposite way. It would be analyzed more detail in following chapters.

It is important to distinguish regional cooperation and regional integration. Regional cooperation refers to policy measures jointly undertaken by a group of countries located within a geographic area. It aims to achieve a higher level of welfare than pursuing such a goal separately. However, regional integration is de facto integration of economies within a geographic region. It may be market-driven integration, that is, there is no explicit agreement or coordinated action among countries within a region to integrate their economies. It results from regional cooperation (Lamberte, 2007). Therefore in this work regional cooperation and

integration would be handled as a synonym terms, although there are small differences between them.

### **1.1 Theoretical Framework**

It was Machlup, who used the integration term in economics literature first time to refer combinations of firms (Jovanovic, 2006: 15). Different from economic integration theories developed after him, Machlup's integration theory had referred integration of competitors and unification of suppliers and buyers not the independent states. Integration of separate states' economies in the literature started to use prior to the 1940s under the name of economic interdependence. At that time economic integration started to be handled as event when two or more states undertake policies that result in greater mutual economic interdependence. By increasing economic interdependence it was hoped that the productive capacity and efficiency of the member states would be increased. There the degree of interdependence varies widely from a reduction of trade barriers on limited number of products to the establishment of a unified economic policy (Hodgson, 1983: 279).

It was only in the second half of twentieth century that economic integration has attracted increasing attention of scholars under the name of "regional economic integration; or "economic regionalism" (Pelkmans, 2004: 3). Actually the conceptual foundations of the theory of international economic integration can be traced all the way back to the classics, but economics and social sciences began to deal seriously with it after World War II (Palankai, 2004: 22). From the 1950s, custom union theories were regarded as the basis of the economics literature on international integration and Jacob Viner appeared as a father of these theories. Viner analyzed advantages and disadvantages of integration in the framework of theory of comparative advantage and his work was known as "static" efficiency analyses theory in the literature. In addition, the integration attempts of recent decades have driven the attention not only of economists and political scientists but also of academics in many other fields, and on this basis many theoretical trends and schools of integration theory have emerged (Palankai, 2004: 24).

In the literature of international economics there is not clearly defined definition of international economic integration (Mikic, 1998: 441). One of the first definitions of integration was given by Tinbergen. To him there are two integrations, negative and positive. Negative integration is “the removal of discriminatory and restrictive institutions and the introduction of freedom for economic transactions” while positive integration is “the adjustment of existing and the establishment of new policies and institutions endowed with coercive powers” (Jovanovic, 2006: 16). Pinder and Kahnert defined economic integration as the process towards the removal of discrimination between the economic agents of the member countries, and creation and implementation of common policies. Mennis and Sauvart were another scholars taking integration as a process, in which boundaries of nation-states become less discontinuous resulting in the formation of more-comprehensive systems. For them, economic integration links up industrial apparatus, administration and economic policies of the member countries. In general, economic integration for Pelkmans is “the elimination of economic frontiers between two or more economies”, for Swann “state of affairs or process that involves the combination of previously separate economies into larger arrangements”, for Maksimova “process of developing deep and stable relationship concerning the division of labor between national economies”, for a Holzman, Marer and Montais “process, in which the prices of all similar goods and similar factors in two regions equalized” (Jovanovic, 2006: 16-19).

Being different from others Drysdale and Garnaut take integration not as a process but as a movement towards one single price for a good and service of factor of production (Drysdale and Garnaut, 1993: 189). Panic (1997) tried to distinguish economic integration from openness and interdependence. For Panic national economy could be said open when it has few barriers for international trade, while interdependence of economy means when economy of each of participating states significantly influenced by the economic situation of the partner country.

However not all of theories could explain clearly about economic integration between the independent states. For example, for Matlli (1999) economists studying regional economic integration look primarily at market relationship among goods and factors of production within the region. They are generally interested in welfare effects

of integration. They do not address questions pertaining to the dynamics of integrations such as changes in the rulers and policies of governing economic region (Mattli, 1999: 19-31).

In addition, economic integration reduces the ability of each member state to follow an independent policy course. It also increases interdependence among the participating among the member states. In order to maximize the gains and to minimize the losses of interdependence the participating countries of economic integration adopt either cooperative policies advancing economic integrations or non-cooperative policies by retracing their steps back to a looser form of interdependence. The advanced forms of economic integration impose constraints on national policies which compel the economic integration to adopt rulers by elaborate new agreements and to set up special supranational institution to administer them. Thus, in the economic integration the member states voluntarily choose to restrict their national objectives and policies or even to replace them completely by targets and policies undertaken in common at the level of union. In other words the progress of economic integration depends on the willingness of the member states to transfer their economic power from themselves to the supranational authority. During the integration process the sovereign power of the member states progressively diminished. It means the power of the union to form and implement common policies increases. The surrender of power and the loss of sovereignty of the national authorities are often strongly resisted. Thus, the process of economic integration generally faced with crisis (Hitris, 2003: 3-4).

Even if the potential economic benefit for the country from the economic integration with other countries might be large, its membership in the union is not necessarily certain. Many countries value their independence and national identity more than the prospect that within economic union, where they might become more prosperous (Jovanovic, 2006). If participating countries act on their own, without the close cooperation with other members of the union, the objective of the union often cannot be reached efficiently. It is important to underline that, despite the fact that the term used as an economic integration, benefits may not be primarily economic. Regions that are economically highly integrated may tend to have less internal conflict. In other words policies that promote trade within the region will affect

intraregional security (Ritzen, 2000: 13). The tariffs preferences that induce regional trade can create powerful income transfers within the region and can lead to the concentration of industry in a single location. The countries that lose income and industry can be sufficiently resentful that separatist movements arise and the overall risk of conflict is increased. The reasons of that sometimes could be unequal distribution of costs and benefits of objectives of union among member states.

According to literature the possible sources of economic gain from economic integration could be attributed to:

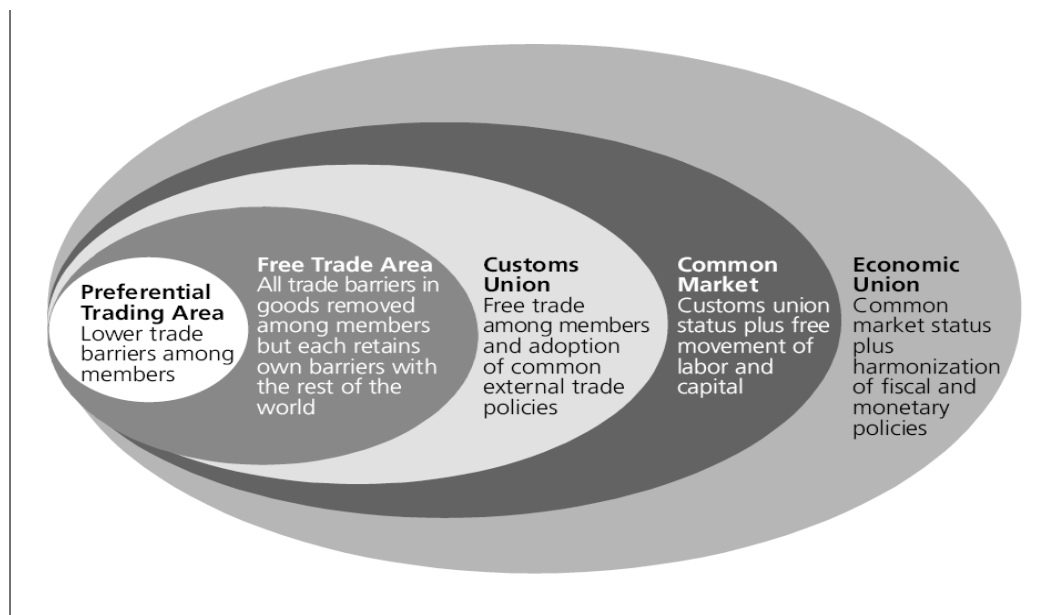
- a. Enhanced efficiency in production made possible by increased specialization in accordance with the law of comparative advantage, due to the liberalized market of the participating nations.
- b. Increased production levels due to better exploitation of economies of scale made possible by the increased size of the market
- c. An improved international bargaining position, made possible by the larger size, leading to better terms of trade (cheaper imports from the outside world and higher prices for exports to them).
- d. Enforced changes in efficiency brought about by intensified competition between firms
- e. Changes affecting both the amount and quality of the factors of production due to technological advances. If the level of economic integration is to go beyond the free trade area and customs union levels, then further sources of economic gain also become possible.
- f. Factor mobility across the borders of the member nations will materialize only if there is a net economic incentive for them, thus leading to higher national incomes
- g. The coordination of monetary and fiscal policies may result in cost reductions since the pooling of efforts may enable the achievement of economies of scale
- h. The unification of efforts to achieve better employment levels, lower inflation rates, balanced trade, higher rates of economic growth and better income distribution may make it cheaper to attain targets (El-Agraa 1997L: 9-10).

There are various degrees of international economic integration between countries. The degree of economic integration depends on the trade agreement between participating countries (Sawyer and Sprinkle, 2006: 185). In addition, these degrees of trade agreements handled as a process leading to cooperation of national economies by other scholars. For example, for Hitris, economic integration might be

understood as a process leading to cooperation of national economies, or as a stage in such a process (Hitris, 2003: 2). The degree of these regional trade agreements between countries or the stage of process tend to change over time (Rivera-Batiz and Oliva, 2003: 549). Therefore in both case, economic integration is often confused with various forms of integration, because economic integration can take many different forms. According to international economic literature, there are four forms of economic integrations, usually considered by the theory of economic integration (Gerber 2005: 23).

- 1) Free Trade Areas (FTA) = free trade between the members;
- 2) Custom Union (CU) = FTA + common external tariffs (CET) on trade with non-members;
- 3) Common Market (CM) = CU + free mobility of factors of production;
- 4) Economic Union (EU) = CM + common economic policy;

Figure 1.1 Stages of Integration and Associated Characteristics



Source: Hodgson, J. S., Herander, M. G., 1983, **International Economic Relations**, Prentice Hall, London, p. 281.

Each of these four levels of economic integration is examples of different kinds of regional trade agreements. However, in the practice not all of accepted

agreements have been put into the practice. For example, in the Europe about 65 % of regional trade agreements currently are in force, not all of them (Gerber, 2005: 25).

### **1.1.1 Free Trade Areas**

According to Dreisen, despite the fact that many things were written about the free trade by scholars, they said little about its definition. By analyzing Smith's, Ricardo's and Sykes's works he suggests two possible definitions of free trade. One might think of free trade as free burdens, a broad laissez-faire principle. One might, on the other hand, think of free trade as free of discrimination (Driesen, 2005: 10). However, to Gerber, in a free trade area, nations are allowed to trade goods and services across international borders without paying a tariff and without the limitations imposed by quotas (Gerber, 2005: 24). From that point of view, the countries agree to eliminate tariffs and other non tariff barriers between each other. The reduction of trade barriers may just cover non-agricultural products as has been between European Union and Israel or it may cover all merchandise trade but not all trade in goods and services, as well as foreign direct investment (Sawyer and Sprinkle 2006: 185).

In the FTA tariff restrictions among member states are removed but each country retains its own national tariff barriers against non-members. The member nations remove all trade impediments amongst themselves but retain their freedom in the determination of their own policies towards to outside world (El-Agraa 1997 and Mikic, 1998). However, in reality, most free trade areas, such as NAFTA do not allow completely free trade. Nations usually reserve some restrictions for particularly sensitive items. With a free trade area, nations usually keep their own health, safety, and technical standards (Gerber, 2005: 24). Preserving of each country its own separate national tariff schedule in the free trade area could result in trade deflection, in a free trade area. "Trade deflection is the diversion of exports to a country within the free trade area that, has lower tariffs on a good" (Sawyer and Sprinkle, 2006: 185). For example, suppose the tariff on car is 12 % in Kyrgyzstan and 100 % in Uzbekistan. The car exporters would sell their cars to Uzbekistan via the Kyrgyzstan. In order to solve this problem, free trade areas and other trade agreements have rules of origin. In addition, free trade area is more likely to command political support from

majority of voters when the partners have similar factor endowments. The reason is that, when factor endowments are similar, the area does not be useful (Rivera-Batiz and Oliva, 2003: 549). The difference of FTA from other forms of integration is that FTA member states take part in international negotiations about trade and tariffs individually, whereas in other forms negotiated as a single unit (Jovanovic, 2006: 169).

### **1.1.2 Custom Union**

Custom union begins with removal of trade barriers among the member states. It also integrates their foreign trade policies by adopting a common external tariff in trade with non-member states (Hodgson, 1983: 279). This would provide member countries a competitive advantage over nonmember countries. However, despite the competitive advantage and removal of trade barriers among member states, free trade in the region continued to be limited, since the member states continue to impose restriction on imports from nonmember nations.

With the time the formation of a custom union may cause fundamental change in the economic structure of the member countries. In the literature these changes are handled as the *dynamic effects* (Hodgson, 1983: 281) of custom union formation. The reduction in the trade restriction between member countries will lead to new competitive environment for many industries previously protected from foreign competition. This competition could cause the usual effect of stimulating efficiency in the previously protected industries. Custom union also may increase the size of the markets for the firms operating within the union. As result, firms could increase their production level. Doing this, they could decrease per-unit cost of production. So the productivity of firms will increase (Hodgson, 1983: 285). That was handled as a two possible production effects, trade creation and trade diversion by Viner (Cooper, 1973: 56). Generally countries formed customs union to abolish trade restrictions within the union. The member states' aims are to implement a unified tread policy towards non-members including a common external tariff on imports.



Factors influencing custom union's affectivity:

- The share of domestic goods. If the share of domestic goods larger and the smaller share of goods imported from non-member countries in total consumption the formation of the custom union will be beneficial for all members.
- The production structure of member states. Countries with similar production structure could replace less efficient domestic production with imports from member countries. Moreover, the greater the cost difference in production for similar goods the greater will be the gains from the customs union. On the other hand if countries' production structures are complementary the formation of a custom union will lead to the substitution of member countries goods for lower-cost goods originating in non-member countries.
- The height of the tariffs certainly affects the strength of the trade creation effect.
- The larger the size of a custom union in terms of area and number of countries the larger effects would be. Since the least-cost producing country will be included in the union.
- Transportation costs also play important role in the efficiency of custom union. The lower the transportation costs are among member countries, *ceteris paribus*, the larger will be the benefits from their custom union. Therefore, it is expected that neighboring countries have better chance of forming a beneficial customs union than far away countries. Transportation costs and other communication costs are the main factor in what is known as the formation of natural trading blocs (Mikic, 1998: 446).

El-Agraa (1997) states that free trade area and custom union is very similar to free trade areas except two differences. First, custom union has a common external tariff. In other words, each country replaces its own national tariffs with common external tariffs. This phase-in may take many years. Almost all trade agreements between countries are "phased-in" over time. In practice, 15 years has become the reasonable limit (Sawyer and Sprinkle, 2006: 207). Second, not all free-trade areas include trade in agricultural products, services, and financial flows.

However, most custom unions include a broad range of international trade. Therefore, the level of international economic integration implied by a custom union

could be said usually deeper than the level of integration implied by a free trade area. Free trade areas and custom unions lead to similar results for an economy and differ only in detail. A custom union not only deals with the elimination of tariffs and quotas and the introduction of the common external tariff but also “with industrial policy and specialization” (Jovanovic, 2006: 318). Custom union also deals with non-tariff barriers and foreign direct investment from partner countries, as well as from outsiders. In addition, the custom union develops a common trade policy, such as common external tariffs, relative to other countries (Marrewijk, 2002: 239). Therefore, making different from free trade area, in customs union trade deflection problems do not exist. In addition, custom union increases the level of protection of those countries, the previously did not have tariffs or whose tariffs were below the level of the common external tariff. According to El-Agraa (1997), the differences between custom unions and free trade areas can be ignored. Free trade areas may result in deflection of trade. If deflection of trade occurs, then the free trade area efficiently becomes a Custom Union. Deflection of trade occur when the cheapest imports from the third countries come via the member country with the lower tariff rate, assuming that transport and administrative costs do not outweigh the tariff differential.

### **1.1.3 Common Market**

Common market is a custom union that allows the free movement of capital and labor. The countries signed the agreement to establish common market continues to maintain a free trade area, a common external tariff allowing the free mobility of inputs, such as labor and capital (Gerber, 2005., Sawyer and Sprinkle, 2003., Rivera-Batiz and Oliva, 2003). For example, the European Community created in 1965, the successor of European Economic Community created in 1957, were custom unions that constituted a limited common market. However, due to the restriction of movements of capital and people the EEC and the EC were not example of perfect common market (Rivera-Batiz and Oliva, 2003: 537).

They are different from other types of integration in that it involves the full integration of both product and factor markets (Mikic, 1998: 461). There, the integration of products are achieved through regional trade liberalization, just as in a

custom union, while, the integration of factors are achieved through the elimination of obstacles to the free movements of factors. That means capital, labor, technology and enterprises could move without obstacles between the participating countries and will encourage both labor and capital to move (El-Agraa, 1997: 57).

However, allowing the free mobility of workers between countries could create some problems between member countries. Since wage differentials among the member countries may include a large amount of migration in the region (Sawyer and Sprinkle, 2006: 185) leading to social problems. Making different from previous types of agreements, such kind of problems resulted in that the common market requires not only the elimination of discrimination against labor from partner countries, but also some degree of harmonization of social policies such as; social security, unemployment benefits, pension funds (Jovanovic, 2006: 318). Therefore, common markets include some elements of economic unions. If the member countries also abolish other differences such as; taxation and product standards, a common market gradually moves to an integrated market (Marrewijk, 2002: 239). In the integrated or common market, workers and firms freely move throughout a region. In this case the Association of South East Asian Nations' free trade is becoming a reality.

#### **1.1.4 Economic Union**

Economic union is the creation, implementation and protection of a single general economic policy in the particular region (Jovanovic, 2006: 169). The difference from common market it includes substantial coordination of macroeconomic policies, including a common currency, and harmonization of national standards and regulations (Gerber, 2005: 24). Around these standards and regulations financial, tax, monetary and other related policies are unified (Rivera-Batiz and Oliva, 2003: 535). By harmonizing economic policies member states go beyond free trade in goods, services, and factors of production. Reorganizing European Economic Community as a Union in 1994 European Union became the example of economic and monetary union. There are two main requirements for an economic union. The first requirement is the creation of a common currency. The advantages of a common currency are much like the advantages of lowering tariffs. Second requirement is that

each national government has to align its national policies with those of the other member countries (Sawyer and Sprinkle, 2003; 185). Beside these requirements member countries should maintain a free trade area, a common external tariff, free mobility of capital and labor, and some degree of unification in government policies and monetary policy. In addition, member states must introduce a central authority to exercise control over these matters so that member nations effectively become regions of the same nations – the EU is heading in this direction (El-Agraa, 1997; 2).

## **1.2 Methodology and Outline**

The analysis of the dimensions of economic integration in the region is based upon analyze of sources focused on regional transition economy, trade and economic cooperation, international cooperation institutions and international organizations. The main method of study included analyzing of sources. Our principal sources included the following: the study of articles, statistics and Internet resources. Also, several resources such as books, journal articles, newspapers and working paper of organizations such as Economic Cooperation Organization, Asian Development Bank, European Bank of Reconstruction and Development, and World Bank will be used. The objective of the thesis is to give an analysis of the most relevant factors that led to the failure of economic integration in the region and new perspectives. Two basic factors are emphasized: economic and political transition and reforms, the complexity of interests between regional and national level.

The thesis is organized in five parts. Following the Introduction, Chapter Two emphasizes historical legacy of Central Asian unity. Here the development of historical common culture and values, economic ties would be discussed in three periodical times; before the Russian Empire period, during the Russian Empire and during the Soviet era. Chapter Three deals with the dimensions of economic integration in the region after the independence. It focuses on development stages of main institutions and programs hold by international organizations evaluating the economic conditions of the region. Chapter Four looks at factors lead to failures and shortcomings of the economic integration in the region. In this chapter it would be tried to find the common points that affected all the integration or cooperation based

institutions' activities negatively. The main questions addressed here is that, is there really any fields that Central Asian states needs integration if there is what it should be like. Finally, the conclusion deals with the new perspectives of cooperation. It evaluates the new economic fields or new approach to old fields that needed not by Central Asian states but Central Asian nations.

## **CHAPTER 2**

### **The Origins of Central Asian Integrity**

Central Asia includes five independent countries; Kazakhstan, Kyrgyzstan, Tajikistan, Turkmenistan and Uzbekistan. Each of these countries has its own political, economical and social policies administered independently. However, until the 1991, when collapse of Soviet Union gained them independence, Central Asia had been ruled generally as a single region under different empires. As a result of each empire ruled over the region, Central Asia had been owned common ethnical, cultural, and social values. Moreover, as results of Russian Empire's and Soviet economic policy, Central Asia's national economies had been parts of single economic structure of USSR. Nonetheless, whether these factors could play encouraging roles in the economic integration in the region after the independence or not is open to discussion. Since, while identifying what belongs to whom these shared values played discouraging factors in the integration after the independence. Therefore it is important to evaluate what kind of common values did they shared in the past and how deep these values affected nations living in the region. In addition, it would also give us light about the economic integration after the independence.

#### **2.1 Common Ties of Central Asian History**

Central Asia's recorded history dates back 2 500 years ago. During this time Central Asia had been home of different empires such as, Persian Empire, Greek Empire, the Kushan Empire, Parthian Empire, Arab Empire, Mongols, Timurids and Russian empire. Despite the fact that at that time some people settled down and built irrigation systems along the rivers, and founded the region's oldest towns and cities, significant part of people who occupied most of the region were nomads (Kort, 2004: 17). When we look at the history of these empires, they did not left concrete common values to Central Asia in terms of unity of region, except last there empire, since, the establishments of each empire were cleaned by following empires in the nomadic civilization. It was strategic importance of Central Asia that empires fought for its

control (Whitfield, 2000: 1-3). Ruling over the Central Asia not all but some empires left some common cultural and social ties to Central Asia that contributed to the strengthening unity of region at this time.

Although trade route have existed in Central Asia as long as there have been people to buy and sell, its development in economic and trade relations took place under the Kushan Empire (Belenitsky, 1967: 97-98). In other words despite the fact that discovery of Chinese silk dates from 1500 BC, the traditional date for the opening of the full Silk Road was 115 BC (Wilson, 2003: 22). The Great Silk Road had become main trade route providing intensive trading relations between the Far East and the West, reaching as far as the eastern provinces of the Roman Empire. It gave to Central Asia vital role as an intermediate link in all international trade by the land route for many centuries. The development of urban was closely associated with the growth of international trade, and the towns became centers of internal as well as international trade (Belenitsky, 1967: 98). Therefore, Kagans consistently showed their interests in its development and trade relationship such a way that trade of silk and other luxury items developed sharply after the diplomatic links were established (Whitfield, 2000: 20). The merchants of the cities and towns became leading promoters of international trade in this period. Goods started to travel in both directions, especially after the Kushan dynasty came to power in Central Asia and ensured stability along the overland route. Under the ensured stability, during the Sogdians became the recognized merchants of the eastern Silk Route. Many of merchants did not travel themselves but instead sent agents along the sections of the Silk Road, from one market to another (Belenitsky, 1967: 102).

Nomads in Central Asia traded their horses for products that they needed, such as textiles, or other luxury goods. Horse also was as once a means of transport and a currency for trade (Chaliand, 2004: 7). Nomads depend on trade and on close relationship with settled peoples. Since, as anthropologists tell us that a symbiosis between settled peoples and nomads was essential for the life of the latter (Negmatov, 1999: 83). The Chinese, for example, traded for silk, tea and grains. The nomads' campaign took place at the end of summer or the beginning of the autumn after the horses had been able to graze their fill and recover from the privations of winter. The

settled people's campaign, by contrast, took place at the beginning of spring when the adversary's cavalry was in a poor state (Chaliand, 2004: 25).

Relationship between nomad and sedentary peoples was one of important factors that affected completeness of region's economy in the history. This relationship can be seen as a relationship between sedentary agriculturalists and pastoral nomad people. However, there are could be different approaches in the literature opposed each other. According to Subtelny "Settled and nomadic people relationship has been characterized most frequently as one of mutual hostility. It was relationship between two diametrically opposed cultures" (Subtelny, 1994: 45). However, these two groups of people entered into close mutual contact through the exchange of products of their respective regimes of production. In return for agricultural products nomads provided products of animals. There were complementary life style between sedentary and nomad peoples lived in Central Asia. Nomads were more dependent on sedentary civilization for the exchange of the products of their regime of production. Therefore in Central Asia the economic ties between the sedentary and nomad peoples were always very close and they were never competition with each other (Negmatov, 1999). They became integrated into one economic complex.

The development of agriculture, mining and the craft industries, together with the expansion of settled people or urban people led in turn to an increase in the exchange of goods between town and country and, between rural and agrarian regions and nomadic steppe. Bread, dried fruit, cloth, weapons and utensils were exported from agrarian regions and towns into the surrounding nomadic steppe. Nomads always needed some products of sedentary economy, such as grain or artifacts, and these were acquired at strategically located market places, through trade. The peaceful method, thus involved exchange of products of the northern steppe and settled towns (Soucek, 2000: 41-43). In exchange, the nomads brought livestock, wool, dried skins to the markets. Even, some towns specialized over particular goods. For example, Bukhara exported fabrics, cloth for use as floor coverings and various carpets. While Samarkand exported brocade, tents, paper and glass and other goods. White cloth, armaments and swords produced in Ferghana (Negmatov, 1999: 83). However, the



foundation of sea faster and cheaper route around the southern tip of Africa had declined the Central Asian economy. Since, for centuries the oases of Central Asia had depended on revenues from trade along the Silk Road. After the discovery of sea route the Silk Road became obsolete.

Many languages were heard and many different peoples seen in their market places- Africans, Semites, Turks, Indians, Chinese, Tibetans and Mongolians. Saying differently Central Asia became one of the trade centers in the Asia that beside different languages used in the region at that time different cultures had clashed. For example, towards the end of first millennium Islam was dominating religion in the region, in spite of that many of its towns were Indo- European in character (Whitfield, 2000: 16).

Coming of Arabs to Central Asia had changed cultural and religious values in the region. In the beginning of eighth, Arab Empire's army took and gradually consolidated their hold on Buhara and Khorezm, cities that considered the most populated and developed cities of the region since the Persian Empire. A Central Asia coalition formed to repel the Arabs, and by the middle of the eighth century, Islam had come to most of Central Asia (Sievers, 2003: 4). While Central Asia flourished at this time, invasions continued. In the thirteenth century Chinggis Khan's armies descended from Mongolia, quickly subdued the entire region, and destroyed much of the region's impressive social and agricultural infrastructure. Entire cities were destroyed, their populations massacred, their vital irrigation works smashed. Whether or not this destruction in the region, done by Mongols, was positive event or not in terms of unity of region open to discussion. Since, as a result of the destruction many Persian cities and learning centers quickened the process that region's population was becoming Turkic rather than Iranian. Iranians increasingly became a minority in a region where they had dominated for at least 1 500 years. The newly arrived Turkic people, who were considered as nomadic people until that day, increasingly become the majority. This ethnic transformation, following Islamization, was a second major social and cultural tie in the history of Central Asia.

When we look at the Mongol legacy in terms of unity of Central Asia, the Mongol conquest was the most important impact on Central Asia people. It can be

consider from two different perspectives. First, as a result of Mongol rule Turkic-speaking people, descendants of whom are now living in Central Asia, started to dominate. Second, Mongol culture and society appear to have influenced the societies of Central Asia. In other words Central Asians started to share same language, Chagatay, and culture. In addition Mongol's support of merchants contributed to the commercial prosperity of Central Asia. According to Rossabi, "The revival of trade was certainly a boon, and Mongol's motive was to generate stability so that the local economy could recover and the Mongols could secure more revenue" (Rossabi, 1994: 29).

A century later, launching from the heritage from Chinggis Khan, Timurlan established an empire based in Central Asia that controlled much of the civilized world. During the Empire of Tamerlane cities in Central Asia were rebuilt. Tamerlane forcibly brought thousands of artisans and craftsmen to his capital city of Samarkand. His empire was the most powerful ever to be based in Central Asia. Tamerlane's cultural legacy was more impressive than his political one. The scholars he brought to Central Asia and the support he gave them initiated a regional flowering of Islamic civilization (Kort, 2004: 29). The next rulers of Central Asia were tribes that collectively became known as the Uzbeks. They arrived as nomads but soon settled down in the main towns of Transoxiana. The single state was controlled the region, but it was undermined by several factors, include the erosion of its economic base. After the Timurlane, Central Asia was controlled by three states: Khorezm, Buhara and Kokand between seventeenth to nineteenth centuries. By this time Central Asia was no longer of any real importance to global trade.

## **2.2 Russian Empire's influence to the integration of Central Asia**

Actually economic relations between Russia and Central Asia date back to around the eighth century. These trade relations were highly developed between eighth and tenth century and the thirteenth centuries. In 1557 after the Russian conquest of the Astrakhan Khanate, both Bukhara and Khariszm sent their embassies to Russian empire, to ask for permission to trade freely in Russia. In seventeenth century the main concern of Russian Empire in the Central Asia was commerce. At that time although

Russian merchants were not trading with Central Asia, Central Asian merchants carried their goods to Astrakhan, Samara, Kazan, Novgorod, the main cities of Russian Empires at that time. In addition, Central Asian states played middleman role between north India and Russia. Therefore, the Central Asian Emirates were important for Russian Empire in terms of trade (Jonson, 2004: 25-28).

The first active Russian interest in Central Asia started during the Peter the Great time. "Peter's interest in Central Asia was equally great. Here his appetite was aroused by exaggerated visions of gold, to be found here" (Sokol, 1954: 21). Although, at that time in Russia, preoccupation with Western questions took most of the attention of succeeding Tsarist governments in foreign affairs there was nevertheless a continued interest in Central Asia. In 1717-18 Peter the Great sent the expedition to Khiva, mission of whom was to establish contact (Sougek, 2000: 197). In 1836 Tsar Nicholas I set up a Special Committee to investigate the conditions for trade with Asia, particularly with Central Asia. Around the same time British textile were only minor threat Russian products in the region. However, in the following years British influence in the Asia expanded. Therefore, around 1840s Central Asia received great attention in the policy discussion of Russian Empire. Although Central Asian's share in Russia's total imports was only about 2.5 per cent at the time, government and business people claimed that it had huge potential (Jonson, 2004: 28-29).

Economic interests were the major factor behind Russia's expansion into the Central Asia. Russia tried to expand its trade with and exports of manufactured goods to the Central Asian markets. Giving priority to economic motivation Russians wanted to gain markets for the products of Russia's growing industry and to acquire sources of raw materials for the industry. Beside this, the nomad areas that were potentially useful for agriculture were highly attractive to Russian. Russians wanted land on which they could grow cotton to supply the country's new and growing textile industry (Manz, 1994: 13). The main Russian economic goal was to increase cotton production. The Russians repaired old irrigation systems and built new ones to supply water to their expanded cotton fields (Kort, 2004; 38). Russians in Central Asia profited from growing cotton. However, in return this, Central Asians lost the

opportunities to grow food locally. Fields that had once produced grains, fruits, and vegetables were converted to cotton, especially in the fertile Fergana valley, forcing Central Asians to import much of the food they ate.

At the beginning of nineteenth century of new trade route to Iran via Turkey for English textiles had been developed. This had become one of motivation factors of coming Russian to Central Asia. Since, new trade route resulted in significant drop in Russia's Iranian trade. In other words Russia started to look for new markets for its growing textile industry. As a result of these developments Tsarist Russia sent some cotton stuffs to Central Asia to evaluate region as a market. According to same source, while the export of cloth and other goods to Central Asia had been growing between 1827 and 1850, the import of cotton increased even more in volume (Sokol, 1954: 20-54).

Uncultivated lands were another motivation factor. Russian rule also has changed the structure of land ownership in Central Asia. Until the Tsarist rule in the Central Asia, land was classified in three major categories: *amlyak*- land belonging to the state, *mulk*- land in private ownership given by the state in return for service, *vakuf*-land given to some mosque or religious school. Russian government owned all land and it became possession of Russian Empire (Wheeler, 1964: 71-79). Had been under same ruler, Central Asia lands first time started to be evaluated in terms of economy as single region. However, in spite of unity of land under one rule, developments over land reflected only Russian Empires interests. Local people's interests were ignored (Brower, 1997).

The irrigated lands were, and continued to be, the most cultivated parts of the settled agricultural areas of Russian Turkestan. During 1870s, in Russian Turkestan cultivated areas compromised no more than 2 per cent of all land. There is not given reliable figures that indicate how much of the cultivated land was irrigated; a rough estimate would be 75 per cent (O'Neill, 2003: 58). These cultivated areas were only a tiny proportion of the total land and they were the most densely populated.

The official policy of government was to foster the transition from a nomad to sedentary life. To turn nomadic peoples to settled one Russian government offered a tax exemption for first five years and half payment of taxes for the succeeding five

years for nomads who would make the transition (Sokol, 1954). In addition, the historical scenario for imperial integration anticipated the gradual evolution of pastoral nomads toward settled farming, and the enlargement of a market economy for agricultural goods (Brower 2003: 75).

As a main motivation of Tsarist Russia and then Soviet Union, cotton has long history in Central Asia. The first great increase came during the American civil war that dramatically diminished cotton supply, and Russian decided to concentrate their efforts on expanding the cotton-growing districts in the Central Asia in order to free themselves reliance on outside supplies. Therefore Russia land reform aimed at increasing the amount of irrigated land. The Russian desire to increase irrigated area was equal to a wish to increase cotton production. As a result of these policies Fergana oblast became one of main cotton supplier center. Although large portion of irrigated land continued to be used for a grain, the area divided to cotton steadily increased from the 1880s until 1917. In this sense, to encourage the trend toward monoculture, Russians in 1893 lowered the freight rate on grain shipped to Turkestan, where Fergana and some other districts had become grain-deficit areas (Becker, 1994: 21-29).

The significance of this change in agriculture production could be seen from this passage “In 1870, Russia imported over 2.5 million pud of cotton, and produced less than 200 000. By 1908, Turkestan alone was producing over 10 million pud, and by 1916 a total of 24 million” (Metley, 1994: 66). Besides focusing on cotton, Russia also paid attention to development of local industry. Since, the region had been seen as raw material resources. At mid nineteenth century the industries of Central Asia were concentrated primarily in the southern part, and in particularly in Uzbek areas. The main branches of the local industry had become the processing of cotton, wool and silk. Some of silk was exported without further processing. For example, “in 1873 Central Asia produced some 4 of 5 million pounds of silk annually, of which 3 million pounds came from Bukhara and Kokand. By 1899 the production of silk reached 76 million pounds, of which 63 millions came from the gubernia of Turkestan” (Metley, 1994: 338).

There is no doubt that the greatest Russian impact on the traditional economy of the Central Asia was in transportation. According to Brower (2003), until the construction of railroad, Russian Empires' all motivations and plans in Central Asia were only a dream. The replacement of the slow and inefficient camel caravan by the railroads opened Central Asia to the Russian merchant and enabled the Russian authorities to transform southern Central Asia into a cotton-growing colony which relied on Russian industry for virtually all manufactured goods. The railroads bound the Central Asian economy firmly to Russia and made significant changes in the region (Becker, 1994). Transportation and development of industry in the region was developed according to location of coal or mineral resources not the locations of ethnic groups lived at that time in the region. For example, the importance of the Trans-Caspian Railroad and the later Orenburg-Tashkent line in the development of Central Asian industry was well illustrated by the fact that "in 1914 about 81 percent of the industry in southern Central Asia was located within the sphere of attraction of the rail way (no more the seven miles from the rail road), and the other 19 percent was mainly in Semirechie" (Matley, 1994: 329).

Immigration of Russian to Central Asia was another accelerating factor of the integration of Central Asia to Russia. The new railroads increased the pace of change and the number of settlers in the area. Between 1896 and 1916, almost one and half million Russians migrated to Central Asia, of whom approximately two-third stayed in area (Becker 1994: 32). Russian and Ukrainian settlers established half a million farms in northern and eastern Kazakhstan between 1906 and 1912. Nomads suffered another way. Nomad's pastures were converted to farms by Russian settlers. The new Russian and local farmers displaced not only Kazakh nomads of steppe, but also Kyrgyz nomads in mountainous areas (Kort, 2004: 39). However, as a result of immigrated Russians and development of railroad, branches of Russian banks opened in Central Asia (Becker, 1994: 30).

Beside these fundamental changes in economic and social structure of region, there were some progresses in daily life developed by Russian that accelerated integration of region. When the Russian arrived in the region there was no modern communication structure and their first step was to create a system of post roads. And

the system of revenue collection was developed. Collected by the authority of the khans or other local rulers there had not been stable revenue collection system until the Russian domination. It was tsarist administration that developed common taxation and revenue collection system in the region (Wheeler, 1964). However, despite these important economic and political changes of the late nineteenth and early twentieth centuries, in contrast to their successor, the tsarist administration did not attempt to alter the traditional social structure or assimilate the local ethnic groups (Fierman, 1991). Tsarist Russia had viewed Central Asia as a single region and not as a region sheltered many ethnic groups. Even it could seen in the Basmachi revolt, which was against Tsarist Russian and Soviet rule at the beginning of twentieth century and in which Central Asian ethnic groups gathered under single unity, Turkestan (Kort, 2004).

### **2.3 Integration under Soviet Rule**

With the collapse of tsarist regime, Soviet rule did not work in Central Asia immediately. In April 1918, when the Turkestan Autonomous Soviet Socialist Republic (TASSR) was established, some of the old tsarist rulers over the territory had been continued (Koichiev, 2033: 49-53). It was during the following decade that some new national units were established. In 1925 political-administrative territories were created- Soviet Socialist Republic (SSR), Autonomous Soviet Socialist Republics, and Autonomous Oblast or Regions, consisting of nations who already possessed a cultural identity, or some groups for whom the Soviet regime created cultural realities (d'Encausse, 1992: 178). In 1937, to Soviet Union new constitution, these national units eventually become The Uzbek Soviet Socialist Republic, the Tajik Soviet Socialist Republic, the Turkmen Soviet Socialist Republic, Kazakh Soviet Socialist and the Kirgiz Soviet Socialist Republic (Anderson, 1997: 26). The outcome was the eventual creation of the five Central Asian republics, each endowed with separate national state institutions within the Soviet Union. These social changes had coupled with the process of modernization, industrialization and collectivization. Moreover, unwritten goals of these policies were to block potential threat of pan-Turkism ad pan-

Islamism. Since there was some Central Asian intellectuals hoped to build the Moslem or Turkic Community (Fierman, 1992: 17).

In addition, the goal of Soviet nationality policies in Central Asia in the 1920s was to create separate national republics. The Soviet Union's policies in Central Asia had two objectives: "to inhibit the potential unification of the region around Turkish-Moslem ideals, and to lay the foundation for its future social transformation" (d'Encausse, 1992: 179). Soviet Union's nationality policy tried to establish separate Soviet republics in the region. Since there was no strong sense of ethnic identity and inhabitants of region often did not consider ethnic borders. They called themselves only by their tribal name or name of town, or simply Muslim. For example, as argued by in Glenn work:

in Tajikistan the Tadjiks did not represents one national entity in an exact sense, because they were divided among a whole range of bekstva and khanates, were separated for one another, and did not have a common economic life. There was no additional market, no economic or cultural national centre. Naturally, the elements characterizing Tajiks as a nation, the language, territory, and cultural unity, were formed and existed from ancient times. But before the Great October revolution these elements were not developed, and existed at very best only potential (Glenn, 1999: 77).

The division of the region along national lines was part of a wider process of separating the region into modernized national entities. For this purpose Stalin's modernization policy was treated separately from the industrialization. Modernization was therefore taken to incorporate such tendencies as: the increase in education amongst populations; the development of the general mass literacy; the improvement in transport links; and the increasing use of communication systems such as print, telegraph, telephone, radio and television to convey information. In other words, "the modernization of the Central Asia society had occurred within the confines of a national state structure" (Glenn, 1999: 78) and in the all modernization efforts had been prepared with regard to Soviet ideology. For example, educational materials used in the literacy campaign were prepared according to Soviet's political nature (d'Encausse, 1992: 190). As Glenn (1999: 73) pointed out, "the process of rapid modernization enforced from the top under Soviet rule had far reached consequences in Central Asia as it altered the economic base, transformed the social structure,



extended the benefits of mass education and communication system to the Asian peoples, and created modern Asian elite”.

Because of the nature of Soviet Union political and economical system, economic issues and decisions became intertwined with national questions. These questions had a noticeable impact on economic policies and the process of its formulation, because economic development of the Central Asian republics was the important part of the Soviet Union. In this sense, it is possible to argue that economic policies were most significant component of the Soviet Union policy. According to Ericson (1992: 240), “the structure and logic of economy, far from ameliorating ethnic and national tensions, at least since 1930s, has systematically distorted interethnic relations, aggravating old animosities and creating new grievances”.

As we have seen above the integration of Central Asian economy to Tsarist Russia had already been begun before the revolution. However, due to advance consequences of the First World War and newly established Soviet system, the process of integration slowed down. By 1921 the soviet leaders had learnt to things from this slow down. The first was that the primary products of the Central Asia were essential for the preservation of the Russian state, and the second that there could be no question of creating a socialist economy until pre-revolutionary level of economy had been restored (Wheeler, 1994: 155-161).

In 1921 New Economic Policy was launched (Granberg, 1990: 121). During the period of the New Economic Policy Soviet republic’s economic councils was responsible for most economic activity, including price control, most of wholesale trade, and the coordination of the activities of nationalized firms, the syndicates, and newly formed trusts. Only macroeconomic planning, state finance, industry of strategic importance, transportation, and communications were directly run from the center, leaving most economic activities in the hands of local activists and national cadre. The private agricultural sector was also naturally in the hands of the local ethnic group. However, decentralization gradually faded in the second half of the 1920s as the Supreme Council of the National Economy assumed more control over the increasingly monopolized industrial sector. Then it rather abruptly ended with Stalin’s collectivization, industrialization, modernization and specialization policies.

According to Stalin's new policies Soviet republics' (local) economic units were held responsible for the implementation of all plans and directives from above, but were not granted any independent control over resource flows or uses (Ericson, 1992: 245). Though local and regional authorities could lobby for resources of changes in decisions, and could represent their regions in the negotiations involved in all planning and plan implementation, they were forced to accept central decisions and implement them as if their own, justifying them to their own populations as both necessary and desirable.

The economic integration of the Soviet Republics into an integral national economic complex has been made possible by the development of economic ties among the republics and the evolution of union-wide infrastructural and economic organizational systems. Each union republic constitutes a complex economic entity, with characteristics processes of reproduction of the population and the labor force and utilizing the natural conditions. Therefore, the economy of the Soviet Central Asian republics became integral component of the single national complex on the USSR (Kasenov, 1998). However, in this complex economic system no union republic can function effectively without broad and diversified relations with other republics (Granberg, 1990: 118).

The creation of multi sector economy in every republic was not accompanied by their economic structures. On the contrary, the predominant tendency was toward a deepening of specialization. The economic specialization of each republic had encouraged bilateral exchange of goods between republics; moreover, ties among republics were closely intertwined with ties among the different sectors and branches on industry (Granberg, 1990). Among the republics productions and resources were so varied that every republic inevitably has some advantages in certain aspects of economic activity. In addition, specialization in the productions or resources but not the processing led to an excessive degree of dependence on the rest of the USSR, especially on Russia. This was strengthened by the employment of large numbers of Russians and other skilled European workers in key sectors of industry. Some have suggested that this amounted to a deliberate strategy designed to ensure continuing political dependence on the Soviet Union (Stringer, 200: 148). Economic ties among

republics evolve in diverse forms. This includes, specifically, the exchange of the products of material production and scientific and technical information, the immigration of the population and the training of skilled personnel, providing commercial and industrial services. The inter republic exchange of the products of the various sector of industry and agriculture were necessary condition and the most important consequence of the territorial distribution of labor in the nation's economy.

Agricultural development during the Soviet period in Central Asia has been to a great extent simply a protection of pre-1917 Russian policy with its emphasis on cotton growing and on withdrawal from raising grain and other foodstuffs (O'Neil, 2003). The shift of some lands from cotton to food crops in the first five years after the revolution caused the production of cotton in Central Asia to fall dramatically by 1921. Did not satisfied with results, Soviet authorities in the 1920s pursued exactly the same agricultural policy as had the Russian empire. The first step of Soviet authorities after the civil war was to restore the irrigation system (Fierman, 1991: 19). The damage to the major canals and other installations was repaired by devoting larger part of land to grain. In other words Soviet policy started to move grain planting from irrigated land to unirrigated areas. In order to encourage this movement, Soviet authorities lifted all taxes on unirrigated areas in 1926 (Matley, 1994: 288). In addition, the cultivated land had been grown. For example, in Uzbekistan cultivated land grew from "1.2 percent in 1928-29 to 68 percent in 1932, and 95 percent in 1937" (Fierman, 1991: 18). Although the organization of agriculture changed the major crop did not changed. Cotton remained the main agricultural production of the local economy. Moreover, the goal of Turkestan-Siberian railroad was to transport Siberian grain to Central Asia. Together with completion of Turkestan-Siberian railroad in 1931, the Southern Central Asia's needs for grain started to be met fully. Even, the priority of agricultural economy in Central Asia had been continued after the Stalin's death. In 1954, Krushchev launched his Virgin Land campaign that aimed to increase grain production. As a result of this campaign northern steppes of Kazak Soviet Republic became unirrigated lands for grain (Kort, 2004).

As it had been in Tsarist Russian Era, during the Soviet time local interests was not considered in the transportation. Local lines were poorly developed, especially in

Central Asia the Soviet rail network did not suit local needs well. Moreover, republic borders were not taken into account. Thus, the railway from Osh, the second largest city in the Kyrgyz Republic, to Bishkek, the capital, passes through Tajikistan, Uzbekistan and Kazakhstan before re-entering the Kyrgyz republic shortly before Bishkek (Pomfret, 1999). The railway lines in northern Kazakhstan were integrated into the Russian network designed to take Kazakhstan's grain and mineral products to Russians markets.

During the first decade Soviet Union devoted less attention to industrial development in the region than agriculture. Between 1922 and 1928, industry in the region barely recovered to the low pre-1917 level. In the following fifteen years, especially during the first two five-year plans there was a great increase in the industrial output and the development of industry related to cotton. Perhaps dramatic changes in industrial development in the region had occurred during the Second World War. Over 300 industrial enterprises were evacuated to Central and relocated according to railway structure, undervaluing states potential or complementary natural resources. The accelerated industrialization of Central Asia begun in Second World War continued into 1950s. Another surge of industrial capacity came in the 1960s, encouraged by Khrushchev's policy, in which individual territorial units were given much greater control over development of their own economies (Wheeler, 1975: 145). During this period chemicals, construction materials, and machine building branches of industry was formed in Central Asia.

In short, when we look at the all developments together towards the end of Soviet Union, the economy of Central Asia was largely based on the extraction of raw materials and the production of agricultural goods and livestock. That is, cotton in the southern republics of Uzbekistan, Turkmenistan and Tajikistan, and grain and livestock in Kazakhstan and Kyrgyzstan, as in the Tsarist period. Oil and gas resources were developed in Kazakhstan and Turkmenistan, and hydroelectricity projects were launched in Kyrgyzstan and Tajikistan. In other words resource based integration was encouraged. However this integration was not only among the regions states, but also among the all union republics.

## CHAPTER 3

### The Aspects of Economic Integration

#### 3.1 Cooperation within the Old Market

The dissolution of Soviet Union, which put an end to the single economic system, not only gave independence for former Soviet Union Republics, it also created much more complex situation than they were expected. Since with collapse of centralized Soviet system deeply connected interstate economic structure and highly interlinked trade system became to the end. Therefore, despite the fact that independence welcomed by all former Soviet republics, they feared the consequences of sharp disintegration. All countries in the area express interest in regional cooperation. The common background of these states did in some ways develop intra-regional cooperation. Additionally, the small scale of national markets, and the lack of direct access to oversea markets led these states to embark on cooperation. It is also important to point out that not all of states in the region was willing to cooperate or was able to follow policies around the cooperation.

##### 3.1.1 Commonwealth of Independent States

The Soviet-Union broke up surprisingly in 1990 giving birth to 15 new nation-states, all of them were previous Soviet Republics. There were, as we have seen above, extensive economic and infrastructural ties between these republics as a requirement of centralized economy. Thus regional cooperation was immediately on the agenda. The primary impetus behind establishment of the CIS was to avert a collapse of inter republican trade by underlining economic, financial, and monetary cooperation between the former Soviet republics. The Commonwealth of Independent States (CIS) was formed on December 8, 1991 by Belarus, Russia, and Ukraine on the basis of the Minsk Agreement. After the thirteen day from this event, twelve newly-independent states, except Baltic states, of the former Soviet Union confirmed and developed the original Minsk Agreement. They adopted the Alma-Ata Declaration and signed the Alma-Ata Protocol to the Agreement Establishing the CIS (Anderson, 1997: 198). According to agreement, the CIS had the following bodies: Council of Head of States, Council of Heads of Government, Council of Foreign Minister,

Defense Ministers, and border Troop Commanders, Inter-Parliamentary Assembly, Executive Committee, Interstate Economic Committee, and Collective Security Council including both Slav and non-Slav former Soviet republics (Dervish, 2005: 214).

Although, the establishment of CIS took short time, during the formation process of CIS there was a great deal of confusion about the sort of organization that the CIS should become. For example, Ukraine, one of the first members of CIS, saw the CIS as a temporary, transitional organization, while for Central Asian CIS was more enduring structure (Olcott, 1996: 23). In other words, new independent states approach to new integration or cooperation organizations have been distrustful from the beginning of their independence. Moreover, at the time the of Alma-Ata Declaration (21 December 1991) that established the CIS, all the signatory states were anxious to promote their individual national interests. The signatories rejected the idea of pursuing a new form of political integration. They, however, strongly support the idea of maintaining coordinated CIS-wide economic integration policies through common monetary, customs, employment, tax and investment policies (Gleason, 2001: 1083).

However, between 1991 and 1993, very little was said about the economic purpose of CIS. Its main focus was military and political issues. The Alma-Ata Declaration of December 1991 committed the CIS simply to cooperation in establishing and developing a single economic space among the member states (Webber, 1997: 50). In the following eighteen month, CIS countries accepted number of decisions, which were less concerned, with laying down a coherent framework of economic integration. This period also characterized by the massive decline in intra-CIS trade, the collapse of common currency and disastrous economic performance indicators for all CIS countries.

As a preventive measure to this economic decline and as a measure to clarify the formal structures of the CIS there were numerous new economic agreements. Promotion of economic integration was issued in May, and this was followed by the signing of an Economic Union Treaty at the CIS summit in September 1993. This Document envisaged the creation of a market-based common economic space by such

means as free trade involving a unified customs regime, a multilateral payments mechanism involving national currencies, transnational ventures in investment, finance and production (Webber, 1997: 50). The aim of this Treaty was to create suitable conditions for the progressive establishment of a free trade association, a customs union, a common market for goods, services, capital, and labor, and a monetary union (Zhalimbetova and Gleason, 2001: 18-19). Although, the treaty was buttressed by a series of implementing agreements on free trade (April 1994), payments (October 1994) and customs (January, 1995), legal harmonization (January, 1996), customs classification lists (February, 1996) and railway tariffs (October, 1996) the leaders were putting into practice divergent policies driven by their own substantially domestic political situations (Gleason, 2001). In other words, the 1993 Economic Union Treaty was only a framework for future action. According to Yeltsin, the president of Russia, in order to work treaty needs some 35 agreements. Some of agreements concluded in CIS summit in 1994. In April of that year a draft agreement on free trade was signed. In the October meeting the Economic Union was established and a payment union was formed. Further a memorandum on “the main directions of inter national development” was adopted (Webber, 1997: 51). After the Turkmenistan’s abstention, Economic Union Treaty lost Ukraine. Ukraine had not become a full member of the emerging Economic Union. It took part in Economic Union as an associate member (Danilenko, 1999: 908). Within a short time, it was understand that these agreements were not enough in order to maintain previous economic relations and to develop closer regional economic integration, because, economies of all these countries had been sharply declining after the dissolution of the SU.

In other words, the formal structures of the CIS were clarified and developed in 1994 after the adopting of 400 documents (Kulchik, 1996). The CIS has become a multipurpose regional organization based on the fairly close cooperation of its members in political, military, economic, social, and cultural spheres (Danilenko, 1999: 897). However, within the few years it became clear that these agreements were not enough in order to develop closer regional integration, especially in the economic field. Therefore, in October 1994, the Council of Heads of State approved the

Agreement on the Creation of the Interstate Economic Committee of the Economic Union. That body became the first CIS organ endowed with supranational powers to carry out a coordinated economic and social policy. Unlike other CIS organs that operate on the principle of “one state—one vote,” the Interstate Economic Committee takes decisions on the basis of a weighted voting system (Anderson, 1997). However, CIS cooperation initiatives were hampered throughout the 1990s, especially by the lack of effective enforcement powers. Intra-CIS trade actually has been declining, whereas trade with the outside world, especially with the European Union increasing (Dervish, 2005: 214).

In addition, immediately after the independence substantial differences among the trade regimes of the transition economies of CIS have become apparent. For example Belarus, Turkmenistan and Uzbekistan followed very protectionist trade regimes while the WTO members like Georgia, the Kyrgyz Republic, and Moldova have liberal trade regimes (Broadman, 2005: 3). Moreover, throughout the CIS region, trade is also impeded by lingering political conflicts resulting from the breakup of the Soviet Union. The unresolved conflicts such as; Nagorno-Karabakh, Abkhazia and Tran Dniester and Osh events have resulted in a breakdown of economic relationships among member states.

Moreover, transition from a centrally planned economy to many national economies moved at different rates. That simply created different types of economic policies. Even small variations among the countries and differences in currency reforms, price liberalization, open trade and border policies, internal democratization, regional security arrangements, investment in regional transport infrastructure, free trade policies and, above all, their approaches to relations with Russia, led to competing tendencies (Gleason, 2001: 1083). For example as seen in following table, all of CIS members have bilateral trade agreement with Russia, but not all of them have among themselves. In addition, despite the fact that there was common CIS free trade agreement, signed by all these countries, free trade among these countries worked bilateral agreement base. Russia has been automatically awarded a leading role in the trade among the CIS (Jonson, 2004: 60).

Table 3.1 Bilateral Free Trade Agreement CIS countries



	Arm.	Azer.	Goer.	Kyrg.	Mold.	Taj.	Uzb.	Bel.	Kaz.	Rus.	Tur.	Ukr.
Arm.	X	No	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	No	Yes
Azer.	No	X	Yes	No	Yes	No	No	No	Yes	Yes	No	Yes
Geor.	Yes	Yes	X	No	Yes	No	Yes	No	No	Yes	Yes	Yes
Kyrg.	Yes	Yes	Yes	X	Yes	No	Yes	No	Yes	Yes	No	Yes
Mold.	Yes	Yes	Yes	Yes	X	No	Yes	Yes	Yes	Yes	Yes	Yes
Taj.	Yes	No	No	No	No	X	No	No	Yes	Yes	No	No
Uzb.	Yes	No	Yes	Yes	Yes	No	X	No	No	Yes	No	No
Bel.	Yes	No	No	No	Yes	No	No	X	No	Yes	No	Yes
Kaz.	Yes	Yes	No	Yes	Yes	Yes	No	No	X	Yes	No	Yes
Rus.	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	X	Yes	Yes
Tur.	No	No	Yes	No	Yes	No	No	No	No	Yes	X	Yes
Ukr.	Yes	Yes	Yes	Yes	Yes	No	No	Yes	Yes	Yes	Yes	X

Source: Freinkman, L., Polyakov, E., Revenco, C., 2004, **Trade Performance and Regional Integration of CIS Countries**, World Bank Working Paper No 38, Washington D.C. 29791., p. 46

Furthermore several CIS members have started to use temporary import bans against selected neighbors as weapons in a variety of bilateral trade disputes or as emergency measures, even if they have signed multilateral and bilateral trade agreements. For example, Russia and Ukraine have engaged in a number of bilateral disputes involving mutual bans of trade in certain commodities, Uzbekistan has cut off imports from the Kyrgyz Republic in retaliation for non delivery of electricity; and Kazakhstan has imposed prohibitive duties on trade with neighboring countries to deal with balance of payments problems (Broadman, 2005: 129). In other words using trade as a weapon in settling disputes has become ordinary issue decreasing workability of CIS. In addition, CIS also includes states that having unresolved problems with of the CIS countries. For example, Georgia followed arbitrary and unpredictable tax administration. The tax code was complex and has changed frequently. Actually it could be said that same thing acceptable for all CIS countries and all these countries allow opportunities to extract corruption. Georgia and Moldova has its own unresolved entities, Abkhazia and Tran Dniester, slowed trade down. These two regions, Abkhazia and Tran Dniester, survive through support from Russia, but continue to exist in a state of political confrontation with Georgia and Moldova, respectively. Due to this kind of disagreement both region have become “black holes” (World Bank, 2004) in terms of formal trade transactions and the location of

enterprises or individuals engaging in criminal economic activity; illegal arms transactions; and smuggling of cigarettes, liquor, and oil products” (Broadman, 2005: 3).

What was important beside this kind of problems partly as a result the underdevelopment of the CIS, and partly due to some internal reasons of member states, the CIS has been accompanied by the adoption of numerous additional agreements establishing different levels of integration between member states. Relating and depending on their new independent economic, political and social policies, the leaders of certain post-Soviet republics started to organize new integration processes within the CIS. Partly, these sort of new organizations were result of internal policies of initiated countries. For example, Nazarbayev put forward the idea of creating a new integration structure on the basis of CIS, the Eurasian Union (Kulchik, 1996: 44). Nazarbayev’s Eurasian Union aimed at introducing common borders and creating super national currency. According to Nazarbayev, this would not mean the destruction of the CIS, on the contrary the Eurasian Union would act as a strong nucleus for integration. When we take internal policies of Kazakhstan into the consideration Kazakhstan needs this kind of union more than any other republic in the region, because of social and economic factors. Kazakhstan has important number of Russian population in the country, and economically Kazakhstan, especially northern Kazakhstan, is deeply tied with Russian economy. However, the reaction of the leaders of the Central Asian republics to the project was contradictory. While Kyrgyzstan supported it, the president of Uzbekistan met it with reserve; “if the Economic Union implied the creation of joint parliament, superstate management structures, and joint citizenship, this would not differ from the USSR. Uzbekistan strongly opposed to turning back” (Kulchik, 1996: 48). Beside this, there were new organizations such as: “customs union” among the Belarus, Kazakhstan, and Russia, EEC, GUUAM, CSTO and CACO. Emergence of such kind of new organizations and differences among the new emerging regimes decreased working efficiency of CIS in the economic field. It became already just a formal organization in the paper. In other words, although at the beginning of the CIS has played a positive initial role in the maintenance of stability of the post-Soviet administrative borders, towards end of

1990s it lost its importance (Bobokulov, 2006: 84), leaving its activities to different organizations within the CIS. As a result it is possible to argue that CIS was just the political instrument of peaceful dissolution of Soviet Union, and formation of small groups of states agreed to cooperate in particular fields. Some of newly independent states displayed their unwillingness to cooperate with former Soviet Republics. For instance Turkmenistan, right the beginning of its independence pursued a policy of neutrality and stayed away from any type of cooperation (Akçalı, 2005: 99). Whereas, Tajikistan could not has used any meaningful initiative and activities for regional cooperation for a long time basically because of the civil war. It means that in the CIS's economic cooperation activities had not reflected all members' interests.

### **3.1.2 Eurasian Economic Community**

After the independence national independence Central Asian states have made number of efforts simultaneously. In terms of economic transition it is possible to identify important trends. First of all the states have tried to join in new word markets. Second they have at large extend presented their old ties with the former Soviet republics' markets in a new social-economic environment. Thus in short time period number of institutions has established or reorganized and renamed. The aims of these reorganizations or renaming within the CIS were to strengthen national independence while facilitating greater economic cooperation.

One of the this kind of reorganizations took place in 2000 in Astana, Custom Union founded in December 1994 by Belarus, Kazakhstan, Russia and joined by Kyrgyzstan and Tajikistan during following years, was reorganized. It was renamed as a Eurasian Economic Community (EEC) in May of the following year (Gürer, 2005). All agreements signed and ratified earlier within the CU framework passed to the successor organization (Primbetov, 2006: 121). Newly founded Eurasian Economic Community's members are Belarus, Kazakhstan, Kyrgyzstan, Russian Federation, and Tajikistan. EEC strategy focused on customs union and on an eventual single currency for the region (Davis, 2006). It emphasized economy based issues more than CIS and was designed to sponsor cooperation in five broad categories; free trade, customs; common market or products; services and labor; and a currency or monetary union. In

May 2002 at the request of the leaderships of Moldova and Ukraine these states were granted the status of observer at the EEC. In 2003 a similar request by Armenia was satisfied. In January 2006 Uzbekistan became a member of the EEC.

The EEC agreement was the result of Kazakhstan President Nursultan Nazarbaev's long-standing vision of close economic integration among the Eurasian states. The agreement was based upon the existing customs union agreements, but was designed as the logical next step in an incremental movement toward policy harmonization. While the community was not intended to limit the sovereignty of its member states, it provided for the delegation to the EEC of some negotiating responsibilities. It was designed to function as a regional international organization, and recognized by the United Nations (Gleason, 2001).

Actually, as will be seen below in transition economies the role of ruling elite was significant in the reorganization and establishment processes. The type of regime economic policies and the way of development of organization strongly depended on leaders of member states (Akiner, 2005: 119). For example, at the beginning of the 1990s, due to Yeltsin's pro-western politics Russia started to loose its control over post-Soviet geography and it was also one of reasons of underdevelopment of CIS, as well. However, Putin have a new life to Eurasian Economic Community. By saying "The CIS countries have many opportunities to carry out large-scale, joint, infrastructure, transport and energy projects. I am sure that their implementation will increase the solidity of our integration, and will provide new opportunities for the Russian Economy and for others besides" (Jonson, 2004: 100-101) Putin gave priority in this area to EEC, and Russia took a leading role in new reorganized Eurasian Economic Community. From that point of view, EEC was partly the product of leaders rather than necessity of transition economies.

Whatever the reasons of establishment of EEC, it was organized to function as a regional international organization, and recognized by the United Nations. The EEC differs from its predecessors in the respect that it has greater enforcement powers than the previously existing customs union had. It is different from previous CIS in terms of decision making process. Decisions in the EEC are taken according to each member's weight. Decision making capacity is weighed with 40% Russia, 20%

Belarus and Kazakhstan each, 10% Kyrgyzstan and Tajikistan each (Gleason, 2001: 1081). The EEC Charter specifies that a vote on major policy issues requires two-thirds of agreement. The voting formula thus implies that, on any given major policy issue, Russia has to take at least two other states support to win a vote. On the other hand, it also implies that Russia will exercise veto power on major policy issues. The organization will be managed through an Inter-State Council, an Integration Committee, an Inter-Parliament Assembly and an EEC Court. However, decision making capacity changed after the participation of Uzbekistan in January in 2006. Decisions are now taken by a two-thirds majority. The weight of votes matches each country's contribution to the Community budget. Russia has 40 votes, Belarus, Kazakhstan and Uzbekistan each 15, and Kyrgyzstan and Tajikistan each 7.5. Moreover, it was designed to function as a regional international organization, not merely as an inter-state agreement like CIS. While EEC is not intended to limit the sovereignty of its member states, it does provide for the delegation EEC of some negotiating responsibilities within international organizations such as the WTO (Zhalimbetova and Gleason, 2001).

Figure 3.1 The Map of EEC countries.



Sources: <http://www.photius.com/eac/> (12.02.2008)

The organization was modeled on other successful regional integration efforts, in particular, North American Free Trade Agreement (NAFTA) (Davis 2006). However, earlier interstate treaties and agreements such as the Customs Union Agreement (1994) have stayed as a basic goal of the Eurasian Economic Community (Zhalimbetova and Gleason, 2001: 18-21). Beside that EEC focused on to establish a common set of policies and standards for coordinating customs and tariffs, visas, payments and settlements, investment, and labor, educational, and health regulations. The main aim of the grouping is a customs union with free movement of goods, services, persons and capital as well as a unified policy on foreign trade, duties, banks, credits and currency (Gürer, 2005). Around these goals and aims EEC tries to coordinate its members integration into the world economy and the international trade system. One of the Organization's main activity vectors is ensuring the dynamic evolution of the member states through coordinating their economic and social reforms while effectively using their economic potentials to improve the living

standards of their peoples. The main principal activities of EEC could be listed as following;

- completing the formalization of a free trade regime in all respects, creating a unified customs tariff and a unified system of non tariff regulation measures;
- laying down the common rules for trade in goods and services and their access to internal markets;
- introducing a unified procedure for foreign exchange controls;
- creating a common unified system of customs regulation;
- drawing up and implementing joint programs of economic and social development;
- creating equal conditions for production and entrepreneurial activities;
- forming a common market for transportation services and a unified transport system;
- forming a common energy market;
- creating equal conditions for access by foreign investment to the sides' markets;
- giving the citizens of the Community states equal rights in receiving education and medical assistance throughout its territory;
- converging and harmonizing national legislation;
- ensuring the coordination of the legal systems of the EEC states with a view to creating a common legal space within the Community (Zhalimbetova and Gleason, 2001).

Among the activities of the EEC particular areas such as; transportation, energy, labor migration and the agro-industrial complex are given priority. In the transportation area organization concentrated on solving the problem of unified tariffs and tries to increase the flow of goods simplifying the customs procedures, completing the intra-state procedures on signed agreements, and creating transnational forwarding corporations. In energy sector members handle jointly development of the hydropower complexes of Central Asia and dealing with the problem of electricity supply and water use. To coordinate the agricultural policies of the EEC states, to create a single food market of the member nations, to reduce the costs of the transportation, storage

and sale of agricultural products, and to establish new market institutions are among the main activities of EEC.

Labor migration has become important issues not only for EEC members but also whole transition economies. In this field, with the adoption and implementation of a program called “Ten steps to Meet the Needs of Ordinary People” (Primbetov, 2006: 121) great progress was planned to achieve. And the social protection of migrant workers, creation of an effective system of regulation and control of the migration of labor resources, and the solution of problems related to the payment of taxes by migrants and their employers has become the main focus of member state of EEC. In accordance with the intergovernmental agreement, citizens of the EEC member states, regardless of their place of permanent residence, have the right to enter, exit, transit, move and stay on the territory of the EEC states without visas (Primbetov, 2006). However, all these agreements work only in the paper, in reality their workability is low. From the point of view of Güler’s work, working over not only economic issues but also over regional border policy matters could made the EEC the most successful inter-regional bodies with a real prospect of being an effective vehicle for cooperation (Gürer, 2005).

In long term, the EEC states are planning to create a full-scale Custom Union including common energy market, and a common economic and custom area. The creation of Custom Union among the member states is now at the first stage, since with the introduction of free trade regime, the EEC states have tried to benefit from its advantages. Internal tariffs for Community goods enable national goods in the EEC to compete with imports. At that time the only three countries, Russia, Belarus and Kazakhstan are largely and economically preferred for the establishment of a framework of possible cooperation. As regards energy cooperation between the EEC countries, the concept of a common energy market is not ready.

### **3.1.3 GUUAM**

When it has become clear that the unwieldy structure of the CIS was ineffective smaller alliances began to form. The importance of these smaller groupings was that, these new organized groupings supported regional integration in different



perspectives. In some points the aims of these small groups contradicted each other. For example, GUUAM was founded precisely to decrease Russia's influence in the region, whereas EEC countries tried to cooperate with Russian market. In result two main states, Kazakhstan and Uzbekistan, in the region had become belong to different blocs in the post-Soviet area. These groups consist of two groups. The EEC includes Russia, Belarus, Armenia, Kazakhstan, Kyrgyzstan and Tajikistan (EEC); the GUAAM consists of Georgia, Ukraine, Uzbekistan, Azerbaijan, and Moldova. As a counterweight the pro-Moscow bloc, the countries of GUAAM are increasingly disposed to demonstrate their devotion pro-Western (Rumer, 2000: 15).

Motivated by their pro-Western orientation, Azerbaijan, Georgia, and the Ukraine decided to form a regional alliance during 1996. One of the main motivations was to benefit from the export of Azerbaijan's oil to Europe through Georgia and Ukraine by limiting Russian influence over the oil export. Later, Moldova joined to this group (Alaolmolki, 2001: 44). On October 10, 1997, the Presidents of Azerbaijan, Georgia, Moldova, and Ukraine met in Strasbourg during summit of the Council of Europe and stated their mutual interest in developing bilateral and regional cooperation. In result, the establishment of the organization was announced in mid-October 1997 by the presidents of Georgia, Ukraine, Azerbaijan, and Moldova in Strasbourg, France. On April 24, 1999, Uzbekistan joined the group at the GUUAM Summit in Washington. Its official purpose was to broaden political and economic cooperation among the member states. In reality, however, the GUUAM countries joined forces in order to work together to break free of Russian influence (Kuzio, 2000). Moreover, Azerbaijan and Georgia's dissatisfaction with Russia's record of mediation and involvement in the Nagorno Karabagh and Abkhaz conflicts added to their desire to cooperate. The Tashkent government also was willing to lessen Russian influence over them and opted out of the CIS Collective security treaty, signed in 1992 by all CIS members except Ukraine. Moreover, although it was not member of GUUAM by following neutrality policy, Turkmenistan demanded from Moscow withdraw the troops that guard the Turkmenistan border in May 1999. Simultaneously, the Turkmen government announced that it intended to sign an agreement with NATO to establish a special program to train military and civil personnel and to participate in

the NATO program “Partnership for Peace”. It appears that Turkmenistan, while not member of CUUAM alliance, made known that its support pro-Western (Rumer, 2000: 210).

The policy of GUUAM was focused on four policy areas: fighting separatism; establishing a joint peacekeeping capability; developing the trade corridor linking Europe to Central Asia through the Caucasus; and finally, facilitating the integration of the member states into “Euro-Atlantic and Atlantic structures”. While the latter aim clearly reflected the hope of seeing a deepening of relations with especially NATO, the remaining three in combination focused on more specific political and economic interests. GUUAM leaders declared their intention to deepen political and economic ties and cooperation, both on a bilateral basis and within regional organizations. The Four countries of the GUUAM association (Georgia, Ukraine, Azerbaijan and Moldova) have created a free-trade zone. However, free trade related policies were not much successful as they expected. Each of the GUUAM countries trade with its partners accounts for only about 2 percent of its total foreign trade, whereas Russia stayed as a main GUUAM countries’ trading partner (Jeffries, 2003). Moreover, the organization’s excessive politicization and economic ineffectiveness nearly prompted Moldova to withdraw from it. It would be much more advantageous for Moldova to pursue closer ties with Russia that to oppose it, if only for the sake of solving the Dniester region. Similarly, in 2002 Uzbekistan announced that it was withdrawing from the alliance of five post-Soviet states known as a GUUAM. While, Moldova expressed doubts as to whether the organization should continue to exist.

During its 6-year existence, GUUAM has pledged to become a vital part of the east-west export routes, although little effort has been shown towards this end. At the 2003 Summit, however, the United States’ commitment was obtained for projects relating to the creation of the Europe-Caucasus-Asia transport corridor (Alaolmolki, 2001: 59-62). However, the realization of that commitment stayed far from reality at May, 2005, when Uzbekistan distanced itself from the Washington and turned its foreign policy towards to Moscow. After 5 months, in Saint Petersburg summit in October 2005, Uzbekistan became member of Eurasian Economic Community.

However, broadening of EEC was not accompanied by deeper economic integration (Pomfret, 2006: 187).

### **3.2 Integration with New Markets**

After the dissolution of the Soviet Union, Central Asian countries have been looking for new partners and new markets in order to develop trade relations beside old former Soviet region. Additionally they need more experienced markets and model economy. In addition, external economic forces also were spending efforts to evaluate Central Asian region as new market and as a supporter of raw-material. These push and pull factors resulted in new establishments immediately after the dissolution of the USSR.

#### **3.2.1 Economic Cooperation Organization**

Economic Organization Cooperation (ECO) was first organization that Central Asia states joined outside of CIS borders. ECO was created in 1985 by Iran, Pakistan, and Turkey for promoting economic, technical and cultural cooperation. In 1992 it was enlarged by Afghanistan, Azerbaijan, Kazakhstan, Kyrgyzstan, Tajikistan, Turkmenistan and Uzbekistan (Gürer, 2005: 17). For the Central Asian countries the ECO was considered as important donor organization doing many, including fundamental infrastructure and communication projects, important for landlocked Central Asia.

The cooperation activities of three major actors of ECO, namely Iran, Pakistan, and Turkey go back to 1955, when pro-Western Baghdad Pact was established (Persson, 1998:114-117). It was turned into Central Treaty Organization in 1959, after the Iraq's left the Pact. After the 5 years with the promotion of Western powers Iran, Pakistan and Turkey decided to extend their economic fields under a new organization, the Regional Cooperation for Development (RCD) (Muni, 2005: 255). The RCD had focused on improving cooperation among these countries in economic fields such as trade, transportation, tourism and natural resources and had produced so many projects which were not realized. As a result the existence of cooperation had been questioned. It was Iran's Islamic Revolution, in 1979, that end up activities of the

RCD. However, the economic cooperation among these countries one more established together with establishment of ECO.

ECO was established in 1985 by Iran, Pakistan and Turkey to promote economic technical and cultural cooperation among its members. Its basic charter becomes the Treaty of Izmir originally signed in 1977 (Pomfret, 1997: 658). In terms its background, the ECO have some similarity to those of ASEAN, as both regional bodies were the result of geo-strategical considerations, to which economic dimensions were added (Muni, 255). The origins of both organizations was not economic integration, instead it was geographical strategic locations and its importance in the regional policy. However, being different from the RCD, the ECO was considered to be independent regional initiative that was not supported by any great power. Despite the fact that it became independent and self controlled organization, the inefficiency of organization continued. For example, under the Protocol on Preferential Tariffs, signed in May 1991, the signatories agreed to offer a 10% preferential tariff reduction on selected items. Application of the Protocol was disappointing; the efficiency of the protocol stayed extremely limited (Gurer 28). However, after the 1992, with its huge number of population and vast areas, considered as a potential market, the ECO was considered as economic potential power (Anthon, 1996: 40-41).

The enlargement of ECO in November 1992 from three to ten members gave the new opportunities for revival of cooperation between Iran, Pakistan and Turkey. The accession of Afghanistan, Azerbaijan, Kazakhstan, Kyrgyzstan, Tajikistan, Turkmenistan and Uzbekistan gave ECO a cultural cohesion, incorporating all the non-Arab Islamic countries of western and Central Asia (Sajjad, 1992: 11). ECO also provides a peaceful cooperation between the original members and newly independent member countries. The enlarged cooperation contains 325 million people spread over almost 8 million square kilometers (Pomfert, 1996: 19), comprising one of the richest parts of the world. It is full of complementarities and potential in terms of the opportunities offered by oil and gas, mineral resources, hydroelectric power and human resources dynamics. Additionally, because of its central geopolitical location,

the ECO and its members, act as an important bridge between east and west and south and north.

Figure 3.2 The map of ECO countries.



Source: <http://www.ecosecretariat.org/> (23.12.2007)

Despite the fact that, ECO was extended to the Caucasus it excludes Armenia and Georgia from the organization. This created impression of new Islamic alliance in the Western countries. Since two of origin countries, Iran and Pakistan, approach to the organization was as a step towards Islamic common market (Sajjad, 1992). However, main purpose of all new members was foundation of new markets for energy and raw materials and transit to world markets, and the development of trade among member (Bhatty, 2002). New members do not welcomed common Islamic market approach, particularly Uzbekistan, having problem with extremism and Islam fundamentalism. Since, the Islamic fundamentalists were supported by Pakistan and Iran (Belokrenitsky, 2005).

In order to conduct activities of these various fields ECO members have committed themselves to establishing four regional institutions (Winrow, 1996: 21):

- Trade and Development bank

- An Reinsurance Company
- An Shipping Company
- An Airline

Despite the fact that to define the institutions was not problematic, to determine their functions and locations of these institutions created difficult situations among members. After long negotiations agreement of institutions location was accepted in third ECO summit in Islamabad, in 1995. According to this agreement Trade and Development Bank would be based on in Istanbul, while Reinsurance Company would be based on Islamabad (Pomfret 1996: 660). It should be noted that locating in the different locations the efficiency of these institutions was not as high as expected.

To promote conditions for sustainable economic development, to raise on this basis the standard of living and quality of life in the member states through mobilization of economic and social potentials of the region, and to remove trade barriers progressively were the main objectives of ECO. With respect to main objectives, fields of activities of cooperation are determined as:

- Transport and Communications
- Trade and Investment
- Energy, Minerals and Environment
- Agriculture, Industry and Health
- Economic Research and Statistics, Project Research
- Education, Science, Culture, and Drugs Control

Among the activities- trade, transport-communications and industry were given as priority fields of organization. For example, at the Islamabad summit the Trade Agreement and an Agreement on the Simplification of Visa for the Businessmen of ECO Countries were main issues of summit. However, these priorities were not acceptable for all members. Eight ECO members signed the Transit Trade Agreement while Afghanistan and Uzbekistan did not sign it. The reasons why these countries did not sing the agreement was not clear, but what was clear was that, the unwillingness of

Uzbekistan and Afghanistan, which lie at important crossroad of the region, was the potential deterrent to intra-regional trade (Pomfret, 1996: 660). Moreover, in August 1992 the Dushanbe-Tashkent railway line was closed to prevent political refugees from entering Uzbekistan. A short time afterward, Uzbek officials closed the entire border between Tajikistan and Uzbekistan, cutting off Tajikistan almost entirely for the outside world (Gleason, 2003: 126).

Trade and investment was another field given priority in the ECO activities. To develop trade member states selected commodities to trade with the low tariffs. Yet, the selected commodities among ECO members were not subject to too much trade between these countries, 10% reduction remained very insignificant for these goods, furthermore it required so many formalities (Pomfret 1996). Thus, the main step towards economic integration, namely preferential trade, was hindered in the very beginning. However, the only reason for not improving in this field was not the selected commodities, newly independent states in harsh economic conditions which required more revenues for economic development were not willing to reduce Customs tariffs. In addition, the long term prospects trade among members seems limited. Since, there was no leading global supplier of consumer goods among the original countries. For example, many Iranian goods on sale in Ashgabat were western consumer goods produced under license in Iran, since the small size of the Central Asian markets are not high priority of transnational firms. In addition, the ECO partners are likely to have difficulty competing with East Asian countries, especially China, in the Central Asian Markets.

Table 3.2. Trade among ECO members (Billion US \$)

	1998	1999	2000	2001	2002
Exports	59.3	68.7	83.2	82.3	94.6
Imports	81.3	75.4	93.0	84.9	103.3
Total Trade Volume	140.6	144.1	176.2	167.2	197.9
Total Exports (Annual % change)	-11.2	16.0	21.1	-1.1	14.9
Intra-ECO Exports*	6.1	5.0	5.5	5.1	5.4
Intra-Trade Ratio* (%)	5.3	5.0	5.3	5.1	5.2

Source: <http://www.ecosecretariat.org/Directorates/dti.htm> (23.12.2007)

After little progress had been made of this front by 1996, the ECO Secretariat took the initiative in trying to reorient attention to include discussion of the implications of the World Trade Organization for the ECO region (Pomfret, 1996: 660-662). In 1999 summit, trade tariffs handled again and signed Trade Cooperation Framework agreement. The ECO member states had made efforts to promote intra-trade and taken significant steps forward for improvement of regulatory frameworks and removal of tariff and non-tariff barriers in the region. The intra-trade ratio of the ECO region (excluding Afghanistan data) in 2002 alike the previous years could not overpass the threshold of 6.0 percent. According to 2002 statistics, the share of intra regional export of Pakistan was just 4.9 percent, Turkey 2.9 percent, Iran and Kazakhstan 3.1 percent and 8.5 percent respectively. While, for Azerbaijan it amounted 7.8 percent, for Turkmenistan 21.3 percent, for Kyrgyzstan and Tajikistan 22.3 percent and 26.6 percent respectively (Orazbay, 2004: 19).

Despite the mentioned despairing background, a new initiative has been signed in 2003, an ECO Trade Agreement (ECOTA), called by ECO Secretary-General Syed Mojtaba Arastou as “the beginning of a new era of economic cooperation among the member states” (Peimani, 2003). Furthermore, in the 8<sup>th</sup> ECO Summit in 2004, it was decided to establish a free trade area within the ECO and the Summit called for urgent implementation of the ECOTA which already included that initiative (Orazbay, 2004). Indeed, this agreement envisaging preferential tariffs among member states meant a



new step towards economic integration. On the other hand, some of member states found itself in another Custom Union process. For example, Turkey has already established a customs union with the EU, and its trade policies and institutions are shifting in order to harmonize better with those of the EU. Because of the customs union with the EU, however, Turkey applies the much lower EU external tariff on industrial imports than ECO tariffs. Turkey also has a free trade agreement (FTA) on industrial products with the European Free Trade Association (EFTA) and has signed 14 other bilateral FTAs, as it tries to harmonize its trade regime with that of the EU (Broadman, 2005).

The situation was not much different in the field of transportation which was a prior agenda item and was also important for the success of trade cooperation. Just in the Ashgabat Summit in May 1992 it was decided that the member states needed transport and communications infrastructure. This issue had vital importance for Central Asian states that were landlocked and required alternative routes that would reduce their dependency on Soviet infrastructure for access to world markets. Tejen-Sarakhs railroad, which would become an integral part of the Trans-Asian railway between Beijing and Istanbul, was planned to build. The ECO plans to build the Andijon-Erjashtom-Kashgar highway, which would become a direct link with China and Pakistan (Kulchik, 1996: 52-53).

Several other projects have been submitted in the fields of road, rail, sea and air transportation. Development of transport plays significant role in the regional cooperation because seven out of ten member states are landlocked countries and remain dependent on transport for developing their economies. Therefore, the high transport costs have been negatively impacting their imports making their exports expensive. For example, the average cost of delivering a 20-foot container weighing 10 tons from Tashkent to Western Europe is approximately 3000 and 4000 dollars. The cost of shipping such container from Tashkent to Milan 3000 dollars. In other words, the high rates of international shipping increase significantly the costs of production by reducing the competitiveness of domestic goods. Thus, for all of Central Asia, the high cost of transportation constitutes one of the key problems, and it severely weakens the capacity of domestic goods to compete on world markets

(Rumer, 2000: 210). Thus, the development of transport system in ECO region has become inevitable issue. In this regard, ECO has attached top priority to the development of efficient and seamless movement of cargo and passengers by road, air, and rail. However, the most important requisite for realization of these projects was the funds that would be provided by the ECO Trade and Development Bank. At the moment the projects which require investment such as ECO Highway that will connect ECO capitals wait for operation of the Bank. On the other hand, Trans-Asia Railway on the Alma-Ata- Tashkent- Tehran- Istanbul route started goods transportation on the existing infrastructure. Another transport project has been the ECO Shipping Company which was established in 1996 between Afghanistan, Iran, Kazakhstan, Kyrgyzstan, Pakistan and Turkmenistan (ECO, Secretariat; 2002). This company already operates with Iranian ships in the Caspian Sea and Persian Gulf. However, for the landlocked Central Asian states efficiency of this company certainly requires integration of sea route with new land infrastructure including both railways and roads.

Diversification of energy transport routes was huge importance for energy-rich Central Asian states. Especially, three Caspian littoral states, Azerbaijan, Kazakhstan and Turkmenistan were looking for alternatives to Russian routes (Rakel, 2005: 252-253). On the other hand, each of three old members of the ECO considered themselves as the new route for transferring Caspian energy to world markets. Common policy within the ECO in this field was problematic in the very beginning since three major actors of the organization competed in this issue and Azerbaijan had serious disagreements with Iran and Turkmenistan about the legal status of the Caspian Sea which was just about to cause military conflict between Iran and Turkey (Nassibli, 2004: 164). Furthermore, great powers such as the EU, Russia and the US involved in the transfer of Caspian energy. Therefore, cooperation under ECO did not yield any result for transportation of energy resources. On the other hand, Turkey was able to take share from the Caspian resources by the support of the US via Baku-Tbilisi-Ceyhan Pipeline route.

Additionally, mutual and cooperation based relations of member states generally do not fit each other. For example, if we look at issue, from the point of

view of Iran's mutual relations, Iran's closest relations are with Turkmenistan. Thus is mainly due to geographic proximity and mutual interests in the exploitation and export of Turkmenistan's oil and especially gas resources. Relations with Kazakhstan are also developing particularly with regard to the oil business. However, Uzbekistan supported the US sanctions against Iran. In 1995-1996 Uzbekistan became the most prominent regional ally of United States. And at the May 1996 ECO Summit Uzbekistan's denunciation of Iran was so vitriolic that the summit ended a day earlier than planned (Promfret, 2006: 185). Uzbekistan openly announced that Iran has been exporting Islamic fundamentalism. Moreover, Uzbekistan tries to distance from Iran also in terms of culture. Moreover, it is undeniable that region's most important cultural center, Samarkand and Bukhara, which are the cradle of Iranian civilization, are in Uzbekistan. Additionally Uzbekistan has a substantial Tajik population, which culturally is the closest to Iran (Rakel, 2005: 252-253).

Despite these many agreements, the ECO record in promoting regional trade is not very impressive. To promote integration, ECO member-countries have to overcome a variety of problems, the most important of which are the absence of a dense network transportation links and limited financial resources. Whatever the reasons of ineffectiveness of ECO activities, the initiatives of member states have continued. Especially, the founding members' efforts to revive the organization have continued. For example, at the eight ECO summit in Dushanbe in September 2004, Iran proposed committing to an ECO free-trade zone by 2015, but no practical steps were taken as previous summits results (Pomfret, 2006: 191). It seems to be like that ineffectiveness of organization mainly resulted from the similarity of the member states' economies, which all tend to be specialized on a small group of primary products, and instability of foreign policies of some newly independent members, which have just started state and nation building process after the 1991.

### **3.3 Integration within the Region**

The dissolution of Soviet Union had the greatest impact on the Central Asian countries. These countries were totally unprepared for dissolution that even afterward the independence some of them did not want dissolution of Soviet Union. Therefore

immediately after the collapse of USSR post Soviet countries showed their desire to gather under one umbrella (Hunter 1996). The idea of creating a community or union of Central Asian states was promoted by applying the simple logic that it was economically and politically more beneficial to deal with weak economies, shared security concerns and common challenges than to deal with these issues individually. Additionally, economic impetus for Central Asian cooperation has derived from efforts to deal with the disruptive consequences of the break up Soviet Union. These developments have required joint action to limit the damage to Central Asian countries.

### **3.3.1 Central Asian Union**

Even before the collapse of the Soviet Union, it was a common practice of the Central Asian leaders started concern about the regions unity and started to hold summits to discuss regional problems (Anderson 1997: 198). The first summit of central Asian leaders took place in Almaty in June in 1990. In this summit the leaders adopted a resolution, the commonality of the Central Asian countries' interests and the inviolability of their national borders (Gleason 2001: 1072) and Kazakhstan joined to Middle Asian Soviet states group and following years it started to use as a Central Asia (Olcott 1996: 52-53). This was an important emphasis on regional integration and the need for further cooperation.

Another main initial step toward to cooperation in the region was made immediately after three Slavic Republics' decision to form a Commonwealth on 8 December 1991. Central Asian leaders met in Ashgabat in order to make decision over whether Central Asian states need to apply for membership to that Commonwealth or not. The outcome of the meeting was an agreement to join in a political community that was geographically defined by the political space of the former USSR. As the USSR was disintegrating in 1991, the leaders of the newly independent states of Central Asia considered the option of creating a regional Central Asian Union in the form of a confederated "Turkestan" (Gleason, 2001: 1072). However, ultimately they rejected this option in favor of conventional. In result, on the 21th of December 1991, eleven former Soviet States met in Almaty and formed Commonwealth of Independent

States. It was at this meeting that the Alma-Ata Declaration was signed, bringing the USSR to an end and legally establishing the post-communist states. During this summit beside the CIS establishment, Central Asian states proposed about establishment of Central Asian Union (CAU) without other countries influences (Anderson, 1997: 138). However, despite the fact that economies of the region were at the top of the meeting's agenda in Almaty regional cooperation, there was no elaboration on how it might be achieved, showing that Central Asian Union was formed just a response to CIS, not due to economic need. Second meeting of CAU took place in August 1991 in Tashkent (Olcott, 1996: 54). However, due to the fighting between Uzbeks and Kyrgyz sides in Osh in 1990 second meeting was not ended with success. This fighting diminished prospect for regional unity of Uzbekistan and Kyrgyzstan reducing trust both sides. However following year meetings between three Central Asian states: Kazakhstan, Kyrgyzstan and Uzbekistan, has continued. By the time 1998 there was held 25 summits in the framework of Central Asian union (Karasar, 2002: 249-290). Tajikistan joined to Central Asian Union in 1998. Until that time Tajikistan could not join due to different reasons, main of which were the civil war and instability in the country. Turkmenistan as a requirement of political system, neutrality, chosen by its president Saparmurat Niyazov, followed its economic and politic policies independently from Central Asia (Turkmenbashi, 1994). Therefore, Turkmenistan has become the only Central Asian state to remain outside sub-regional organizations, such as EEC, CACO, and SCO (Bohr, 2003: 16).

Each of these 25 summits had its significance in cooperation and integration of Central Asia, some of them was very important in terms of development of regional integration. For example, in the Tashkent meeting in 1993 the leaders of Uzbekistan and Kazakhstan announced the formation of the new union- the Commonwealth of Central Asian States. According to this new union new market would be formed on the territory of the five sovereign countries. New market would include common customs and duty relations, taxation, a joint defense zone, and jointly coordinated prices, even common currency implementation was taken under consideration (Kulchik, 1996: 49). However, establishment of the Commonwealth of Central Asian States was not occurred. It stayed just as a part of temporary policy. Instead of Commonwealth, after

the series of meetings during 1993, customs union was established between Kazakhstan and Uzbekistan in January 1994 (Hunter, 1996: 102). The two countries agreed to abolish tariffs between themselves and to create a common market by the year 2000. According to the agreement, if implemented, it would provide for free movement of goods, services, capital and labor between Uzbekistan and Kazakhstan and would establish coordinated policies for credit, finance, budget, tax, customs and duties from 1994 until 2000. This agreement was described by Kazakhstan's President Nazarbaev as "abolishing borders between the two countries" (Gleason, 2001: 1075). However, same year on 22 March, Nazarbayev in conference in London contended that increased Western investment toward helping to stabilize Kazak's currency and finance by destroying agreement coordinated currency and finance policies with Uzbekistan (Alaolmolki, 2001: 43).

In April in 1994, Kyrgyzstan joined in Union. Turkmenistan again has not been involved in these efforts. It followed basic foreign policy principle conducting relations with Central Asian on a bilateral basis (Hunter, 1996: 101). During 1994 the Inter state Council was designated as the principal deliberative organ and responsible for coordinating the economic policies. The CAU was viewed as a forum for resolving disputes within Central Asia, and also as a vehicle for promoting collaborative projects. The promotion of collaborative projects would require investment, and thus one of the main positive initiatives of the CAU was the establishment of Interstate Central Asian Bank of Cooperation and Development, which was founded in June 1994 with head office in Almaty and branches in Bishkek and Tashkent (Rumer, 1996: 44). In the 1990s the Bank granted several small credits, such as 300 000 American dollar to an Almaty firm producing electric meters 300 000 to an Uzbek firm producing blood products, and 300 000 American dollar to a Kyrgyz firm manufacturing electric motors. The modest scale of these credits illustrates that the Bank was playing a primarily symbolic role. By January 1997, the member countries had given the Bank only some two-thirds of its charter capital, and it was clearly incapable of drawing substantial external funds into Central Asia for investment in collaborative projects (Pomfret, 2006: 188).

Among the significant summits with regard to Central Asian region was the thirteenth summits of Central Asian leaders, held in 1995, CAU's agenda had shifted from economic issues to security (Karasar, 2002: 264-267). As a result of seventeenth summit of Kazakhstan, Kyrgyzstan and Uzbekistan the Central Asian battalion established as a joint peace-keeping force of the Central Asian Union. This battalion located in Kazak-Uzbek border and was send to the NATO military exercises that took place in North Carolina in the same year. After the this summit, one could say that the priority field of union had altered. In addition, the market formed by the union has stayed too small and intraregional Central Asian trade has continued to decrease. Trade data show that total exports from the five states amounted to 13.78 billion American dollar in 1996, a full 1.5 times increase over the 1994 level, however, intraregional exports over the same period actually fell from 2.1 billion to 1 billion American dollar (Tang, 2000: 369). Apart from its security activities, the CAU had little in the way of practical achievements. Officials claimed to have made dome contributions in tax harmonization and elimination of double taxation, but these are difficult to document, and the CAU had little impact on intraregional trade (Pomfret, 2006: 188).

The twenty-third Central Asian summit was held on January in 1998 in Ashgabat with basic objective of persuading Turkmenistan and Tajikistan to join the Central Asian Union. At this summit, which was attended by all five leaders, the Tajikistan's president Rahmanov announced his country's desire to become member. However, Niyazov did not display any interest in joining in. In the twenty-fifth summit of Central Asian states on July in 1998 in Chophon-Ata, Tajikistan joined in CAU and Central Asian Union was reorganized as a Central Asian Economic Community (CAEC). Around main policy of CEAC the leaders agreed on to focus on a Central Asian common monetary policies and to improve intra-regional trade. However, following years the CAEC quickly expanded into security and military cooperation, as well (Swanström, 2004: 44).

### **3.3.2 Central Asian Cooperation Organization (Central Asian Economic Community)**

One of the main summits in the framework of CAEC was organized in Almaty with the participation of Nursultan Nazarbaev president of Kazakhstan, Askar Akaev president of Kyrgyzstan, Imomali Rahmonov president of Tajikistan and Islam Karimov president of Uzbekistan. According to Karasar (2002) the importance of this summit was that the CAEC had adopted a Strategy of Integrated Development for the period 2000-2005, with the priority goal of forming a common economic space. The strategy focused on creating quadripartite interstate consortiums in such key economic sectors as irrigation and hydropower, oil, gas and metallic ore extraction, crop cultivation and investment banking. However these strategies faced with three main obstacles: first, the countries' inability to resolve bilateral differences, owing to their quest for unilateral short-term advantages; second, mutual insolvency and lack of internally generated capital; and, third and most fundamentally, the search by all these countries for long-term economic partnerships with more developed countries outside the region and indeed outside the CIS. According to Karimov's opinion after the that summit, the CAEC had in many ways repeated the experience of the CIS. More that 250 CAEC decisions adopted but not implemented, and another thirty-four agreement was under consideration with no better prospects. Many of the CAEC's documents have proven as totally redundant as those of the CIS, Karimov concluded.

As a result of ineffectiveness of CEAC the four leaders reestablished the CAEC as Central Asian Cooperation Organization (CACO) in February 28, 2002. Central Asian leaders have attempted to distinguish CACO from its predecessor by emphasizing improved effectiveness. Following year agreements and multilateral treaties signed under CACO modeling a sort of EU model (Karasar, 2002: 285-291). However, CACO's activities were also focused on security and maintaining stability in Central Asia, not on the economic cooperation. The results have been Discouraging and it also showed us that Central Asian states were not ready for a formalized organization with such a potentially strong influence over their economic policies. Uzbekistan is, for example, viewed by the other Central Asian states as a potential hegemonic power and CACO is considered to be a tool for control over the region



(Swanstrom, 2004: 44). Moreover CACO has not contributed to multilateral dialogue, but is more of an organization that simplifies bilateral consultations rather than improves multilateral ones.

After the establishment of CACO important meeting was held in 2004 in Almaty. A number of agreements were signed, including closer coordination in combating terrorism and drug trafficking, as well as the creation of various consortia that will deal with such issues as water, energy resources, and food supplies. In this summit Russia suggested to become a member of the Central Asian Cooperation Organization (Gürer, 2005). During the following summit held in October same year in Tajikistan, reflecting on the changing geopolitical environment in the region, Russia joined the CACO. However, Russia's membership in the Central Asian Cooperation Organization is unlikely could renew that organization (Olcott, 2005: 211). Moscow has little interest in having multilateral economic relations disrupt bilateral economic relations with various CACO member states. A year later together with Uzbekistan's entry into Eurasian Economic Community (EEC), CACO was effectively merged into Eurasian Economic Community, putting the idea of a Central Asian regional community temporarily on hold (Dadabaev, 2007).

According to Olcott, there are few common issues among these leaders, but that does not diminish the common problems that these states need to address. Many of these problems are best handled on a regional basis. However, each Central Asian leader believes he knows better than his neighbors how to handle these common problems, so most solutions are being developed in isolation at the national level with only limited regional or international engagement (Olcott, 2005: 212). The five presidents have competed among themselves for international preeminence, with the rivalry being especially keen among Islam Karimov of Uzbekistan, Nursultan Nazarbayev of Kazakhstan, and Saparmurat Niyazov of Turkmenistan. The difficulty of cooperation is further impeded by Turkmenistan's policy of "positive neutrality" which Niyazov has interpreted as preventing membership in regional associations (Ibid: 211). Additionally, Central Asia's leaders have substituted virtual cooperation for real economic cooperation; the CACO lacks authority and institutional capacity to manage economic relations among the member states. Annual summit meetings are

also held, more as a forum for communication than decision making. In addition, they are likely to become less frequent when the current group of presidents and their administrations has little experience about the cooperation.

### **3.3.3 Cooperation Organizations around Caspian Sea**

Iran as a key regional player was the first country to show interest and act upon over Caspian Sea Cooperation Organization. Within the framework of an intergovernmental conference organized in Tehran in February 1992, Iran as an organizer, put forward the idea of forming an organization that would oversee cooperation in the Caspian region. Shortly afterwards, Iran, Turkmenistan, Kazakhstan, Azerbaijan and Russia established the Caspian Sea Cooperation Organization, whose main focus has become the development and utilization of the Caspian Sea (Shirazi 2003). One of the main objectives of newly organized cooperation was to establish reliable links between the ports of the Caspian Sea and the Iranian ports of the Persian Gulf (Mozaffari 1997: 183). If they had succeed in implementing that plan, today not only energy but also commercial flow to and from Central Asia would be altered dramatically. However, as have seen in other organizations, CSO also has become ineffective during the realization of its activities. At present Caspian Sea energy exports and, Central Asian exports and imports almost go through northern trade corridor. Moreover, there was a passage mentioning that taking main role in the establishment CSO Iran has tried to counterbalance Turkish influence in Caspian Sea through the Turk Cooperation and to have an important say in the delimitation of the Caspian Sea (Gürer, 2005). In other words, CSO also was part of one of leading countries policy.

One of the main reasons why Central Asian economic integration efforts were not successful as expected were that Central Asian countries joined to different integration institutions goals of which sometimes contradictory. For example as have mentioned above Caspian Cooperation was established as counterbalance Turk cooperation in which took place all Central Asian countries (Gürer, 2005: 17). However, Turkic Cooperation created in 1992 by Turkey and comprising the Turkic-speaking former Soviet Republics Azerbaijan, Kazakhstan, Kyrgyzstan, Turkmenistan

and Uzbekistan was the single organization in the region based on common ethnic and cultural values beside economic interests. In terms of that The Turk Cooperation had chance to become important organization in the region. Since it has one more plus, social and cultural aspects, comparing other organizations (see more detailed information (Ball, 2000). The Turk Cooperation handled as a Turkic Summit. For example, in the Winrow's book the summit of Turkic language speaking countries was handled as a Turkic Summit (Winrow, 1995).

Conference on Interaction and Cooperation in Central Asia (CICA) was another institution that concerns Central Asian Cooperation. It was initiated by Kazakhstan in 1992 elaborating along the example of the OSCE confidence building and conflict preventing measures in Central Asia and its surroundings. The "Almaty Act" of 2002 can be considered the ground work for the creation of a real international organization. Besides the four Central Asian states also Afghanistan, Azerbaijan, China, India, Iran, Israel, Mongolia, Pakistan, Palestine, Russia and Turkey are the members of conference. The CICA agenda concentrates on security issues, disarmament, nuclear weapons free zone and stability questions, against separatism, illicit trafficking. Thus, although this conference does not have economic interest, it could support Central Asian Economic cooperation indirect way by strengthening security in the region (Gürer, 2005: 16).

### **3.4 International Organizations supported Cooperation Programs**

Beside the cooperation and integration efforts of Central Asian states in the region, there are some international programs and projects that supported by international organizations and concentrated on development of Central Asia's economic infrastructure in regional base. The are generally focused on expansion of regional trade, and possibly long-distance transit trade through development of transportation network, coordination of regional resources most notably energy and water resources, expanding private sector and advance growth of economic activity throughout the region.

### **3.4.1 Central Asian Regional Economic Cooperation Program**

The Central Asian Regional Economic Cooperation (CAREC) Program is an Asian Development Bank supported program created in 1997. ADB initiated this program to encourage economic cooperation among countries in the Central Asian region. The Program addresses one of the most serious challenges of the region, a remote location. It focuses on large infrastructure needs and cooperation in transport (especially road transport), energy (including the water-energy nexus), trade policy, and trade facilitation (especially customs cooperation) (Pomfret, 2006: 194).

The Program consists of ADB's member countries in the Central Asia region, namely: Azerbaijan, People's Republic of China (focusing on Xinjiang Uygur Autonomous Region), Kazakhstan, Kyrgyz Republic, Mongolia, Tajikistan and Uzbekistan. ADB has tried to make strong relationships with each of these partners focusing on the region's long-term development needs (Kuroda, 2006: 24).

Initial activities of program concentrated on identifying infrastructure requirements and policy issues relating cross border trade and traffic. All these activities performed in a series of five workshops in 1998, and the findings of those studies were reviewed and policy issues were pursued with the participating governments. The first workshop tackled the challenges and opportunities in transportation and, the second, in energy. The third and fourth workshops covered cross-border trade cooperation between Kazakhstan and the PRC, and the fifth workshop deliberated on Kazakhstan-Kyrgyz Republic trade cooperation.

Since the beginning program continued activities by promoting policy reforms that would remove cross border barriers to both goods and people. The program has stressed to develop connectivity, competitiveness, and community in the region through the development of subregional transport infrastructure and market-driven economic integration. By aiming to improve connectivity, to simplify rules and processes, to establish a regional energy supply market program has been providing the foundations (Butiong and Davis, 2007). The work involves the preliminary analysis of previously identified high-priority infrastructure investments such as the rehabilitation and improvement of the interconnected power grid of Central Asia and

the development of various inter country transport corridors. Workshops in 1999, furthermore offers the opportunity to widen the initiative to promote economic cooperation in Central Asia with the recent membership of Tajikistan in ADB.

In September 2000, the high-level regional transport conference was held, as a result of which the implementation of key projects was endorsed. The main projects were;

- regional railway improvement for the Northern Tajikistan railway;
- road rehabilitation of the Almaty - Horgos road;
- rehabilitation of the Lugovoy - Bishkek - Balykchy rail line;
- construction of Uzbekistan - Kyrgyz Republic - PRC railway (for which a working group already exists);
- rehabilitation of the Dushanbe - Sarytash road;
- Rehabilitation of Southern Transport Corridor Road (Kyrgyz Republic) (\$32.8 million) (expected completion: 2009). Rehabilitation of the road linking Andijan, Uzbekistan; Osh, Kyrgyz Republic; and Kashgar, People's Republic of China;
- Almaty-Bishkek Regional Road Rehabilitation Project (Kyrgyz Republic) (\$5 million) (ADB/TRACECA) (completed in 2005). Rehabilitation of the Bishkek–Geogievka road and two bridges, improvement of customs facilities, and construction supervision;
- Dushanbe–Kyrgyz Border Road Rehabilitation (Tajikistan) (\$15 million ADB, and \$6 million OPEC Fund) (expected completion: 2008). Rehabilitation of 140 km of the Dushanbe–Nurobod section of the Dushanbe–Kyrgyz border road, and 77 km of rural roads serving poor villages (Asian Development Bank, 2005)

In order to realize these projects between October 2000 – June 2005, ADB approved 11 loans totaling \$275.1 million for seven CAREC-related projects, and leveraged co financing in support of these projects totaling \$140.7 million and to further regional cooperation, a field office in Almaty, Kazakhstan, was opened in November 2004. During this period, ADB also approved 23 technical assistance grants

totaling \$17.4 million. In 2003, the Program expanded to include the European Bank for Reconstruction and Development, International Monetary Fund, Islamic Development Bank, United Nations Development Program, and World Bank (Asian Development Bank, 2005). These financial institutions have become co-financers of projects. Despite slow progress since its launch in 1997, CAREC established a Trade Policy Coordinating Committee in 2004. This was an important step made by CAREC towards trade facilitation among CAREC members.

Trade facilitation remains critical for CAREC countries due to unstable regulations, bureaucratic procedures, and low-quality infrastructure. It is particularly important because most CAREC countries are landlocked and shipments have to overcome long distances and multiple borders. Accordingly, the physical and administrative conditions of each country in the region are essential, particularly a transit country, affect all others (Elborgh and Sadikov 2007). Therefore, cooperation seems to be inevitable for the region states.

### **3.4.2 Special Program for the Economies of Central Asia (SPECA)**

The Special Program for the Economies of Central Asia (SPECA) was launched in 1998 with the support of two United Nations regional organizations, the Economic and Social Commission for Asia and the Pacific (ESCAP) and the Economic Commission for Europe (ECE). The presidents of Kazakhstan, the Kyrgyz Republic, Tajikistan and Uzbekistan signed the Tashkent Declaration on 26 March 1998 creating SPECA (Pomfret 2006: 189-190). The same year in September Turkmenistan officially indicated its intention to sign the Declaration and to participate in SPECA projects. To support the Central Asian countries in strengthening their cooperation in order to stimulate economic development and facilitate integration with the economies of Asia and Europe was defined as the main purpose of SPECA. Through consultation with the participating countries, five priority areas were identified and working groups set up as instruments to develop and implement the program in each priority (<http://www.reliefweb.int/library/documents/2002/icg-uzb-30may.pdf>).

The international conference was held among SPECA member countries with participation of international financial institutions in Astana, in Kazakhstan, on 25–27 May 2005. In the conference participants underlined the requirement of economic cooperation, as it is a key precondition of development of the SPECA countries. According to them, sub regional economic cooperation would be important step towards to rapid transition to full-fledged market economies, and more rapid integration into the world economy. For member countries, SPECA provides key support for economic and environmental cooperation among its members, their integration into the world economy. By them the SPECA work plan for 2005–2007, stronger economic cooperation with regional and international organizations have been welcomed. The SPECA member countries emphasized that the proposed SPECA projects and activities reflect their technical cooperation needs in transport, water and energy use, environment protection, trade, and have their full support. The SPECA member countries called on international financial institutions and UNDP to take full advantage of the collaboration between the Central Asia Regional Economic Cooperation Program and SPECA.

Beside SPECA program UNDP includes another regional development programs as well. Being different from first two, third regional program document (2006–2010) of UNDP for Europe and the Commonwealth of Independent States (CIS) places an important focus on Central Asia with programs to promote regional cooperation. In the next 4 years, UNDP’s assistance in the region will continue to focus on: economic reforms, democratic governance, environmental sustainability, and conflict prevention and preparedness. In addition, The Silk Road Area Development Project (SRADP) of UNDP also has taken steps to encourage regional dialogue on priority issues affecting transit, customs, trade, and investment. In 2003 UNDP also started to implement the EU border management program for Central Asia.

### **3.4.3 TRACECA**

TRACECA is an interstate program aimed to build an international transport route from Europe to Asia through the Caucasus and Central Asia. The program objectives were formulated in 1993 at the Conference in Brussels ( Brussels

Declaration, 1993 ) by the European Commission and the Governments of Armenia, Azerbaijan, Georgia, Kazakhstan, Kyrgyzstan, Tajikistan, Turkmenistan and Uzbekistan to support their integration into the international economy by improving and enhancing trade and transport. It was supported and financed by international institutions such as World Bank, European Development Bank and Asian Development Bank together with related states (Olcott, 2005: 210). For example, the European Bank for Reconstruction and Development (EBRD) have committed funds for capital projects on ports, railways and roads along the TRACECA route, the World Bank (WB) have financed new capital projects on roads in Armenia and Georgia, the Asian Development Bank (ADB) have allocated substantial funds for road and railway improvement and the Islamic Development Bank (IDB) had invested into development of the transport sector in the TRACECA countries. The program's priority was given on regional goals and projects generally focused on regional base.

#### Objectives of the TRACECA

- program stimulating co-operation among the participating states in all matters related to the development and improvement of trade in the region;
- promoting optimal integration of the international transport corridor Europe-Caucasus-Asia "TRACECA" into Trans-European Networks (TENs);
- identifying problems and deficiencies in the region's trade and transport systems;
- promoting TRACECA projects as a means to attract funding from IFIs, development partners and private investors.
- defining, in terms of contents and timing, a Technical Assistance Programme to be financed by the European Commission (EU).

The First Annual Meeting of TRACECA program held in Tbilisi on March, in 2000. Heads of Governments, Transport Ministers and Vice Ministers of Armenia, Azerbaijan, Bulgaria, Georgia, Kazakhstan, Kyrgyzstan, Moldova, Romania, Tajikistan, Turkey, Ukraine and Uzbekistan, as well as Representatives of the



European Commission attended this meeting. During this meeting the Inter Governmental Commission rules of procedures and Basic Multilateral Agreement on International Transport for Development of the Europe- the Caucasus-the Central Asia was adopted (Erdal, 2004).

By the 2007, the five annual meeting has been hold. Among them Third Annual Meeting was more beneficial than others. In that meeting not only ministers and high-ranking officials from 12 participating countries, but the representatives of the European Commission, other international organizations like UN ECE, ECMT, World Bank, EBRD and others attended. Attendance of such kind of international organizations made program's activities more active. Since some of these international organizations have inclination to fund projects. For example, in 2005 ADB has become one of main institution funding program. The focus of the Fifth Annual Meeting of the IGC is the adoption of a strategy for the development of the Europe-Caucasus-Asia transport corridor until 2015 and of the TRACECA region connections with the trans-European networks. The strategy makes provisions for the institutional evolution of TRACECA into an international organization that will finance itself and its projects ([http://igc.traceca-org.org/english/igc\\_docs/mla\\_eng.pdf](http://igc.traceca-org.org/english/igc_docs/mla_eng.pdf)).

According to Lyudmila Trenkova, Secretary General of the TRACECA Permanent Secretariat, from the beginning of program 115-120 million euros have been utilized under the TRACECA. Lyudmila Trenkova said 2006 would be the last year of the program, which will continue its development as an international organization and will self-support itself. Today the annual contribution of each participating country is 50000 euros. Projects under the program will continue to be implemented for another two years after it is physically over. Initially, it was designed for the former Soviet republics. Its successful development since 2000 logically attracted Bulgaria, Romania and Turkey (Trenkova, 2006). A project for the training of forwarders is being carried out at the moment.

## CHAPTER 4

### The Reasons of Inefficiency of Economic Cooperations

#### 4.1 Economic Factors and Cooperation

Despite the fact that Central Asian republics were part of one unified centralized economy and inherited slightly similar economic structure, after 1991 they went to different directions by following different economic policies. This was due to a combination of factors, complicated by the power struggle between political, economic, and regional fractions within each republic and due to difference of economic and social development level of countries (Anderson, 1997). The economic structure and the priorities of reform in transition economies were another economic reasons resulted in different economic policies.

How deep trade dependence was in the Central Asia? This could be examined in two ways, as have analyzed in the Grafe's work (Grafe, 2006). Firstly, it could be analyzed by comparing with other regional trading blocks around the world. Intra-regional trade in the EU accounts for over 60 per cent of the total exports, within the NAFTA this ratio is 58 per cent, and among the ASEAN and Mercosur members, regional export makes up more than 20 per cent of total exports. Even, being region of small economies the Black Sea Economic Cooperation, which is included previous Soviet Republics, has important ratio accounting some 15 per cent. Comparing with these regions Central Asian intra regional trade shows very low level, accounting around 5 per cent. Secondly, by comparing the intra regional trade divided by Central Asian the importance of regional could be analyzed. Intra regional trade divided unequally when we look at the country level. The difference are very striking, in Kazakhstan, exports to other Central Asian countries accounted for just 3 percent of the total in 2001 decreasing from 6 percent in 1995, while in the Kyrgyzstan this figure as high as 30 per cent felling down from 47 per cent. Similarly Kazakhstan receives only around 3 percent of its imports from other Central Asian countries, while Tajikistan receives close to half of all imports from the region. Uzbekistan takes a middle position, while Turkmenistan does not appear to be highly integrated with the rest of Central Asia. The asymmetry in dependence of regional trade creates a problem

for discussions on regional cooperation, because incentives to cooperate are clearly unequal (Grafe, 2006).

However, this comparison ignores the key geographical characteristic of Central Asian countries, being sandwiched in between some of the largest countries, Russia to the north, Iran and Turkey to the west and China to the East. At the same time, this location gave them opportunity, if they could behave as a one region in terms of economy and trade. Russia is a major trading partner for all five Central Asia republics and particularly for Kazakhstan, a reflection of the Soviet legacy but also of geographical proximity (Grafe, 2006: 158). China accounts for around 7 and 9 per cent of the total trade of Kazakhstan and Kyrgyzstan. In order to benefit from these largest countries all Central Asian countries should behave side by side. However, they could not do it owing to different reasons, analyzed in detail following pages.

By analyzing different cooperation institutions Broadman concluded that successful regional integration can only be achieved if the countries involved a minimum of economic, and political common ties (Broadman, 2005). From the point of view that, the inefficiency of Central Asian economic cooperation has viewed as a normal. However, despite the fact that ECO members are a politically diverse group of states ranging from secular Turkey to religious Iran, the ECO activities has faced with difficulties. Turkey, one of the leading country among the members, has been focused integrate with Europe not with the ECO members. For example, in 2004 Turkey, already a WTO member, formally became a candidate for EU accession. Turkey has already established a customs union with the EU, and its trade policies and institutions are shifting in order to harmonize better with those of the EU. Turkey also has a free trade agreement (FTA) on industrial products with the European Free Trade Association (EFTA) and has signed 14 other bilateral FTAs, as it tries to harmonize its trade regime with the EU (Tang, 2000: 369). In other words, as have mentioned previous paragraphs the priorities of economic policies of member countries are the important factor in the success of cooperation.

What was the complementary level of the Central Asian and co member countries economies? To start with ECO, despite the fact that most of ECO members can be considered semi-industrialized economies, all of these economies concentrated

on primary products or textiles and clothing. For example, exports of Turkmenistan, Iran, Azerbaijan and Kazakhstan are dominated by oil and natural gas, which made them competitor in the energy market in Eurasia. Cotton is the major export of Uzbekistan and Tajikistan and important for Turkmenistan. It also the biggest primary export product of Pakistan, on the other hand. For Pakistan and Turkey, manufactured exports are more important than primary products, but in both countries there is a heavy concentration on textiles and clothing. Moreover, Central Asian road and rail networks were constructed with a northward orientation, towards Russia and Ukraine, while the three regional members' transport networks were directed away from the USSR (Pomfret, 1997: 661) which makes their national economies far from each other. It seems difficult to cooperate trade among these countries in short period of time.

If we evaluate ECO as a single market, it gives prominent market with 300 its million population and numerous natural resources. However, at the ECO members vary considerably in size, population and living standards as a result of which national economic priorities and policies change. Additionally, biggest parts of members are lower-income or lower middle income countries according to the World Bank categories, although none are among the least developed economies. Afghanistan and Tajikistan still suffer from internal disruption. Moreover, Afghanistan has poor social indicators with a high illiteracy rate 71% of adults while six former Soviet republics have high literacy rates. If take into the consideration Joseph Nye suggestion, a favorable integration conditions are more likely when there is more symmetry or economic equality among potential member states (Sadri, 1997: 575), it also seemed difficult to establish efficient cooperation structure.

Table 4.1 GDP of ECO member countries per CAPITA (\$ US)

	1996	1997	1998	1999	2000	2001	2002
<b>Countries</b>							
Afghanistan	n.a	n.a	n.a	n.a	127	116	174
Azerbaijan	410	505	562	574	655	704	753
Iran	1,632	1,874	1,293	1,434	2,054	2,238	1,769
Kazakhstan	1,351	1,446	1,469	1,129	1,230	1,492	1,645
Kyrgyzstan	387	374	341	252	278	309	323
Pakistan	488	475	470	445	394	422	477
Tajikistan	183	159	221	179	159	169	189
Turkey	2,880	2,948	3,093	2,764	2,943	2,149	2,608
Turkmenistan	425	546	592	757	933	1227	1,520
Uzbekistan	599	625	625	702	559	466	384
ECO							
Average*	1,231	1,294	1,212	1,151	1,211	1,111	1,144
World							
Average	5,072	5,089	5,012	5,122	5,190	5,085	5,202

Source: <http://www.ecosecretariat.org/> (04.11.2007)

If we take the CIS or Central Asia countries, they produce roughly the same set of goods and as a consequence the market lies. The market formed by them is too small and intraregional Central Asian trade has been decreasing as a result of economic policy priorities. Trade data show that intraregional exports fell from 2.1 billion to 1 billion American dollars between 1994 and 1996 (Tang, 2000: 366). Within the transition period not only intra regional trade fell down, but also the level of trade with Russia also decreased. According to Rumer, the decline in economic relations between Russia and Central Asian states was due to the fall in production activity, and to the reorientation of resources toward domestic markets. There were also other serious obstacles impeding commercial ties between Russia and Central Asia. The lack of a reliable economic system for payment transfers among countries, the instability and limited convertibility of national currencies, and the very weak instruments for enforcing compliance with the terms and conditions of contracts. Another important factor is the declining interest in each other's products because of the competition of superior goods, technologies, and services of firms from outside the CIS (Rumer, 1996: 33). Neither Russia, nor the other countries can compete with these outside firms. One way or another all of these economic and social factors played main role in the determination of economic policy.

Were not able to compete with outside market qualities some of Central Asian countries started to follow import-substituting economic policies. Turkmenistan and Uzbekistan implemented their import-substituting industrialization policies in 2002 through the introduction of trade restrictions such as import licenses, government certificates, and limits on hard currency sales. As a result of unstable national economic policies, it seems difficult to see efficient economic cooperation in the region in the short period of time.

#### **4.2 Political Regimes and Cooperation**

The leaders of the eleven states who came to Almaty to form the commonwealth of Independent States on 21 December 1991 pledged themselves to the creation of democratic and law-governed states. However, in practice these leaders presided over considerable continuity in institutions. In other words cooperation in Central Asia has become a state centric process, representing the interests of personalist regimes and even individual leaders, rather than between states and societies (Bohr, 2004: 498). In other words it was the leaders of Central Asian states that played a key role in shaping the emerging polities and institutions (Anderson, 1997: 86). In all these states small group of authoritarian ruling elites has been the key role in shaping the emerging political and economic orders. In addition, ruling elites have been unwilling to create regional organizations which affect their newly won sovereignty (Bohr, 2004: 501). For example, in Turkmenistan and Uzbekistan the option was for authoritarianism, with former's choice embodied in the personalist rule of Saparmurat Niyazov. As a result, despite the fact that it was formally a member of CIS and the ECO, Niyazov has rejected nearly all regional initiatives. Like Niyazov, Uzbekistan's president Karimov justified his authoritarian rule in terms of the overriding need for political stability in his country (Anderson, 1997). Most important, there is a growing division between the region's two competing policy orientations, namely those of the pro-reform countries (Kazakhstan, Kyrgyzstan) and the state-oriented countries (Turkmenistan and Uzbekistan) (Gleason, 2001: 20). Tajikistan's approach was somewhere between these two groups.

Among the Central Asian states, Kazakhstan and Kyrgyzstan have become more pro-reform countries. They have adopted a tradable currency in November 1993, liberalized prices and started privatization of major sectors of the economy including industry, telecommunications and energy by encouraging and supporting regional cooperation. Especially, Kazakhstan has viewed itself as the initiator of cooperation as a result of perception that has been reinforced by the country's central geographical location (Bohr, 2004: 499). Actually, the formation of CIS Custom Union and its reorganization as the EEC was a partial realization of Nazarbayev's proposal. Kazakhstan, even initiated the establishment of Conference on Interaction and Confidence-Building Measures in Asia (CICA), which has modeled on the OSCE. Kyrgyzstan generally was the supporter of Kazakhstan, since its northern regions linked to world markets through the Kazakhstan (Gleason, 2001). Although Kyrgyzstan followed more liberal regime in economic sector supported Kazakhstan, in the political sector it was difficult to define its position. Since, Kyrgyzstan is physically divided between the northern and southern regions, with the northern region linked to Kazakhstan and the world economy and the southern region inevitably linked to the Uzbekistan economy by geography, infrastructure and culture. Therefore, Kyrgyzstan's regime faced with complex political situation (Bohr, 2004: 499). Yet in the economy sector these regimes have moved quickly to create a reasonably stable legal and regulatory structure for commerce establishing the framework for commercial transactions and property rights. They also formed the framework for a new system of government, a new tax code and a new system of tax administration Kazakhstan adopted a modern banking system, a securities exchange system, bankruptcy legislation and a system of public utilities management. (Gleason, 2001).

Uzbekistan and Turkmenistan followed authoritarian regimes which is the opposite of other Central Asian countries economic policies. Economic policies in Uzbekistan and Turkmenistan in particularly discouraged the establishment of small and medium sized enterprises, thereby preventing the formation not only cooperation in the region but also formation of traders and business class that would trade with neighboring countries. For example, in mid 2002 the Uzbek government imposed high

rate of taxes on private imports, effectively bankrupting the countries' shuttle trade and destroying many small businesses (Bohr, 2004: 497). Uzbekistan's variant of welfare authoritarianism, with its government-controlled prices and strict controls on foreign currency, banking and trade, has created severe policy incompatibilities in the Central Asian region. In July 2000 Uzbekistan took the unusual step of adopting an additional level of visa controls, stepping out of the "unified Soviet visa regime" which previously made it possible for all former Soviet citizens to move from country to country with passport alone, by requiring that even Kyrgyzstan and Tajikistan ordinary residents apply for a visa to cross into Uzbekistan (Gleason, 2001: 25). When we take into consideration that, Uzbekistan lies at center of region's trade transportation network, visa control implementation was not only discouraging or preventing factor, but also ending point of trade among Central Asian states. In other words, regional improvements in transport, energy use, sustainable water policy, communication, currency, the trade environment and the movement of people dependent upon policy decisions in Uzbekistan (Gleason, 2001).

Additionally, Uzbekistan and Turkmenistan have implemented number of artificial barriers to the flow of goods and people. It is notable that these two states have only natural resources based trade with other Central Asian states, while exports from Kazakhstan and Kyrgyzstan are relatively well diversified, including agricultural products and some manufactured goods and natural resources (Grafe, 2003). Beside this, Uzbekistan's strengthened border regimes have affected entire region, especially for Kyrgyzstan and Tajikistan, whose export to Europe and Russia must travel through Uzbekistan. The tariffs charged by Uzbekistan approach 20 per cent, approximately twice the level of those imposed by Kyrgyzstan and Tajikistan (Bohr, 2004).

What was important about the Turkmenistan, it puts less emphasis on Central Asian regional cooperation and more emphasis on relations with the Caucasus, Iran and Caspian egress routes. Since, major trans-Asia ground transport routes pass from Turkey and Iran, through Mashhad to Ashgabat and Tedzhen in Turkmenistan before going on to other major Central Asian capitals and the Far East (Gleason, 2001).

Tajikistan stayed between these two type regimes. Under Rahmanov's regime the Tajikistan government agreed to undertake a comprehensive program of structural



reform. The priorities of comprehensive reform were fiscal reform; currency reform, and energy sector reform. Tajikistan like other pro reform countries in the region, claimed to support the principle of free trade with neighbors (Gleason, 2003: 91). However, economic isolation, mountainous geography and poorly developed physical infrastructure make Tajikistan one of the world's most remote and difficult to integrate economies. Therefore, president Emomali Rahmonov's reform strategy is dependent upon improved cooperation with the Central Asian neighbors (Gleason, 2001). The small size of domestic markets, the small service sector, and the country's unavoidable dependence on a limited number of primary commodity exports, in particular cotton and aluminium, make increased trade a necessity for economic recovery. However, Uzbekistan government actions have been preventing the external trade of Tajikistan. The border with Uzbekistan has been closed by Uzbek government, cutting off Tajikistan almost entirely from the outside world. Custom and duty stations were constructed at every border checkpoints. In other words, it seems to be like that cooperation or economic integration actions in the region dependent on regimes' desire, which are completely differ from country to country, not region's desire.

Beside these, substantial differences among the trade regimes in the region some of these regimes have used temporary import bans against selected neighbors as weapons in a variety of bilateral trade disputes or as emergency measures. For example, Uzbekistan has cut off imports from the Kyrgyz Republic in retaliation for Non delivery of electricity; and Kazakhstan has imposed prohibitive duties on trade with neighboring countries to deal with balance of payments problems. Using trade as a weapon in settling disputes is counterproductive and tends to hurt both countries in the dispute (Broadman, 2005: 129).

All southern Kazakhstan obtains its natural gas from Uzbekistan, but towards end of 1990s has suffered from periodic interruptions in the delivery of this fuel. The disruptions were due to the question of payment. Tashkent demands that natural gas cost be paid in hard currency, but Kazakhstan proposes barter. This conflict came to the point where, in the spring of 1999, southern Kazakhstan was left without natural gas. Apparently the ruthless behavior of Kazakhstan in the rail transit issue was a response to Uzbekistan's own refusal to compromise on the question of payments for

natural gas. Uzbekistan also regularly cuts off the delivery of natural gas to Kyrgyzstan, there by causing serious difficulties in the latter country (Rumer, 2000: 13). As a response Kyrgyzstan also uses its natural resources. For example, Kyrgyzstan shut off delivery of irrigation water to the southern Kazakhstan in the spring of 1999. Kyrgyzstan did it so after Kazakhstan failed to delivery coal to Kyrgyzstan. It was requirement of agreement between these two countries. Kazakhstan also owed Kyrgyzstan millions of dollars for electric power. In turn, Kazakhstan has it is own reasons. Kyrgyzstan did not pay for the railway movement across Kazakh territory. Although the governments after these events have resumed its delivery of water, the fundamental problem-mutual nonpayment persists.

Moreover, as a result of choice of ruling elite two main states of the region, Kazakhstan and Uzbekistan, became two different blocs in the Post-Soviet realm towards end of 1990s. These blocs consist of two groups. The first includes Russia, Belarus, Armenia, Kazakhstan, Kyrgyzstan and Tajikistan. The second consist of Georgia, Ukraine, Uzbekistan, Azerbaijan, and Moldova (GUUAM) (Rumer, 2000: 13). These differences could be seemed in economy field as well. Uzbekistan's national development strategy emphasized the maintenance of local industrial capacity, full employment, rural development and diversification of the economy through foreign direct investment. To achieve these objectives, Uzbekistan maintained price controls and industrial subsidies. In contrast, Kazakhstan was making a determined push towards the market, as we have seen. Consequently, Kazakhstan was being pressured by Uzbekistan to slow down on price liberalization while Russia was urging it to go faster.

What about ordinary people, the survey of 2067 people in 1993 in Uzbekistan and Kazakhstan showed that about one in ten felt their countries should rely on other Central Asian countries, while some half preferred go alone (Spechler 2000). In addition, nations of states in region have fed wrong perception about the union, inherited from the Soviet Union. Generally these kind of perceptions were the results of inexperience in the mutual and regional cooperation.

### **4.3 Ethnic Issues and Cooperation**

As Swanström has noted, even if Central Asian states have argued that they have strong national identity within the current stated borders, the current states are weak and the national identities are not strong enough to create effective and solid states. Therefore, all states tried to strengthen its national identity (Swanström 2004).

Being results of Soviet nation policy there was created more than hundred ethnic groups, which is continued to be much apparent within the region. During Soviet period, rather than generating and creating a sense of common national identity and blunting ethnic, tribal, and regional differences nation building policy and cultural development added new layers of division to those already existing in the Central Asian societies (Hunter 1996: 10). The negative effects of this legacy were obvious during the perestroika and glasnost, when cultural grievances and rivalries erupted into open and inter-ethnic tensions and clashes increased. In the post-independence period cultural issues have remained controversial and divisive, showing that, under Soviet rule, ethnical conflicts and tensions were frozen, rather than resolved (Mozaffari 1997: 25). For example, there are three societal resources that may possible challenge the dissatisfaction of these states: ethnic, sub-ethnic and supra ethnic identities (Glenn 1999: 141). With the decline of the Soviet empire, these conflicts floated back to the surface, leading to the dissatisfaction of states, discouraging the regional cooperation.

Today, all five Central Asian states are multi-ethnic. The number of ethnic groups in any given Central Asian state ranges from several dozen to more than one hundred. Especially, the Fergana valley in particular presents a complicated mix. In the Kyrgyz part of the valley there are concentrations of Uzbeks. For example, in the Osh, a town of Kyrgyz, Uzbeks constituted about 50 percent of the town population (Jonson, 2004: 162). In the Tajik part of valley the Uzbeks make up a very large share of the population. There are also large concentrations of ethnic minorities outside the Fergana valley. In Uzbekistan, Bukhara and Samarkand historically and culturally constitute Tajik cities with a mainly Tajik population. Kyrgyz population can be found in Pamir, Tajikistan, close to the Kyrgyz border. In addition the existence of enclaves in neighbor countries further complicates the ethnic picture. When someone looks at this ethnic picture could thought that this it should accelerate the cooperation among

the states. Its intermixed ethnic character should help to bring the region closer economically, but it has worked opposite way as a result of policy priorities of governments in the region (Byrd, 2006: 15).

In other words, Central Asian authorities have implemented their nation-building policy such a way that it affected not only related nation but also neighbor country's policy as well. For example, Turkmen-Uzbek relations deteriorated after the December 2002, due to Turkmen authorities' behavior. They forcibly relocated ethnic Uzbeks in Turkmenistan living near the border to Uzbekistan (Jonson, 2004: 163). A Turkmenization process of ethnic Uzbeks in Turkmenistan continued, while there was a parallel process of Uzbekization of Turkmens living in near the border of Uzbekistan. Another example, the Uzbek populations in Tajikistan, over one million, and Kyrgyzstan, over 500 000 Uzbeks, have already started to call for union with Uzbekistan (Aydin, 2000: 18). According to Aydin, these Uzbeks motivated not only by ethnic ties, but also by Uzbekistan's growing economic and strategic importance. In return, approximately one million Tajiks and just under a million Kazakhs live in Uzbekistan. If they also started call with titular nations it may be result not in cooperation, but in conflict between states. In other words all these facts played as main factors of discouraging cooperation, instead of being encouraging. Additionally, the Central Asian states show a great reluctance to being part of homogenous region. For example, Uzbekistan is a most reluctant of all states in the region owing to its multiethnic society and the need to distance itself from the other states in order to reinforce its Uzbek identity. Not only Uzbekistan, but also all Central Asian states would prefer not to be part of Central Asia and become dependent on it, because all these states want to protect their national characteristics (Swanström, 2004: 42).

Although extensive common heritage of the region seemed difficult to separate what belongs to one nation from what belongs to another the Central Asian regimes has focused on to differ specific characteristics of one nation from the other nations in the region. Tajikistan is in the process of creating a national identity and for this purpose focusing on the national culture, national identity, and national language, for instance (Jonson, 2006: 167). Thus the ongoing nation and state-building process is itself a major factor preparing the ground for disintegration of region. Moreover,

giving priority to nation building process in their policies for Central Asia countries national economy policies and activities stayed under influence of nation building policy.

Central Asian states tried, not only go away from each other, but also from their minorities. For example, the non-recognition of Russian language as a state language and the demands by some Kazakhs for the Russians to leave Kazakhstan has fuelled antagonism between the two groups. Similarly in Kyrgyzstan there is a large Russian presence, constituting 17 per cent of the population. The tensions between Kyrgyz and Russians do not appear as great as between the Russians and the Kazakhs but tensions have been deteriorated by the ousting of Russians from influential jobs (Glenn, 1999: 142). Thus it could be said that, national minorities in the region are under pressure of the nation and state building process. For instance, the share of the Uzbek population in Tajikistan fell from 24 percent in 1989 to 15.3 percent in year 2000. A similar development has taken place in Uzbekistan and other Central Asian countries. The reduction can be partly explained by migration but also by people choosing to define themselves as belonging to the titular nation in order to avoid problems (Jonson, 2004: 163).

In addition to, the challenges of economic and political transformation, Central Asian states have had to contend with national identity. In the first day of independence, they faced with necessity of replacement of soviet ideology and its social and economical model with a new one that could also help them to define their separate “identities”. About that issue Kortunov and Lounev wrote that “in all Central Asian republics the non-indigenous population has been systematically forced out of government, industries, education and the higher echelons of the army. For example, at the parliamentary election in Kazakhstan in 1994, the Kazakhs, who made up forty percent of the population, won 63 per cent.” (Kortunov and Lounev, 1998: 94). The Russian language has been consistently forced out. Only in Kyrgyzstan has teaching in the Russian language in school and universities been maintained at the same level.

Moreover tribal, clanic and regional allegiances still exist within the titular nationalities of the region. Not only have these sub-national identities persisted but social position within the region reflects the traditional hierarchy of these tribes and clans. For instance, in respect to Liu's study, there are three major problems challenge inter-ethnic harmony in the region (Liu, 1998: 82-84). First there is the rise of ethno-nationalism in Central Asia. In other words, the imposing revival of national culture after the independence of region's states could be seen as an expression of an assertive ethno-nationalism. Second, tensions and conflicts between ethnic groups are exacerbated by the stark disparity in their social and economic conditions. For example, in Kyrgyzstan there is a clear economic disparity between the North and the South. While the Slavic population is relatively concentrated in the economically more developed North, the economically less developed South is mostly inhabited by Kyrgyz and Uzbeks. Third, problems in inter-ethnic relations in Central Asia are compounded by factors and elements beyond Central Asia. Sometimes these states face a crisis because of rising social and economic tensions, mass unemployment and impoverishment of the population, and growing conflicts among ethnic and clan groups (Burnashev, 2002: 144). Although, historical tensions between ethnic groups far from now, there are periodic increases in tensions between Uzbek and Tajiks, Uzbek and Kyrgyz, Kazakhs and Kyrgyz. For example, a village situated between Kazakhstan and Uzbekistan, a Bagyz village, created tensions between these two countries in 2002. Uzbekistan wanted to return the territory in question despite the fact that its residents want to be incorporated into Kazakhstan. Fed up with Kazakhstan's feeble support and Uzbekistan's unwavering resolve, the village declared itself the independent Kazakh Republic of Bagys in an attempt to motivate the Kazakh government into resolving the dispute (Farrant, 2006: 71).

The disparity between ethnic and state boundaries, difficult questions of property distribution among the ethnic groups, and the presence of economic inequality arguably have made it easier for nationalism to emerge. Moreover, new national symbols and myths have emerged. The year-long celebration of the millennium of Manas, the legendary warrior and founder of Kyrgyz people, and Tamerlan as a founding father of Uzbeks, and the re-discovery of various national writers,

historians and scientists are the prominent examples of creation of nationalism. The establishment of national identity diminished the reemergence of inter-regional identity. State-less nationalism, each with its own cast, has been the norm and has been received much more focus than regional integration projects (Kubicek, 1997: 647). However, it should be noted that, all these things were not result of unwillingness of regional integration rather they were result of natural process necessary to state building policies.

#### **4.4 Underdevelopment of Border Crossing and Transportation Network**

The border issues have historical explanations that stretch over centuries and cultures, but these were undervalued by the unnatural creation of the current Central Asian states in the early 1990s. The region had been markedly mixed and no ethnic group has a large or clearly defined area that they have controlled for any long continuous period of time (Swanström, 2004: 42). However, when the Soviet Union dissolved in 1991 the national borders of Central Asian republics have automatically become the border of new sovereign states. Showing just new administrative and political boundaries, the new borders of these states have become meaningless in terms of economic and social issues. Since, by creating of five Union Republics in the Central Asia rather than a single Turkestan, the purpose of Moscow was to easy control over the region by dividing them with irregular and sometimes economically irrational borders (Spechler, 2000). However, the new internationally recognized borders cut up Soviet made up economic unity.

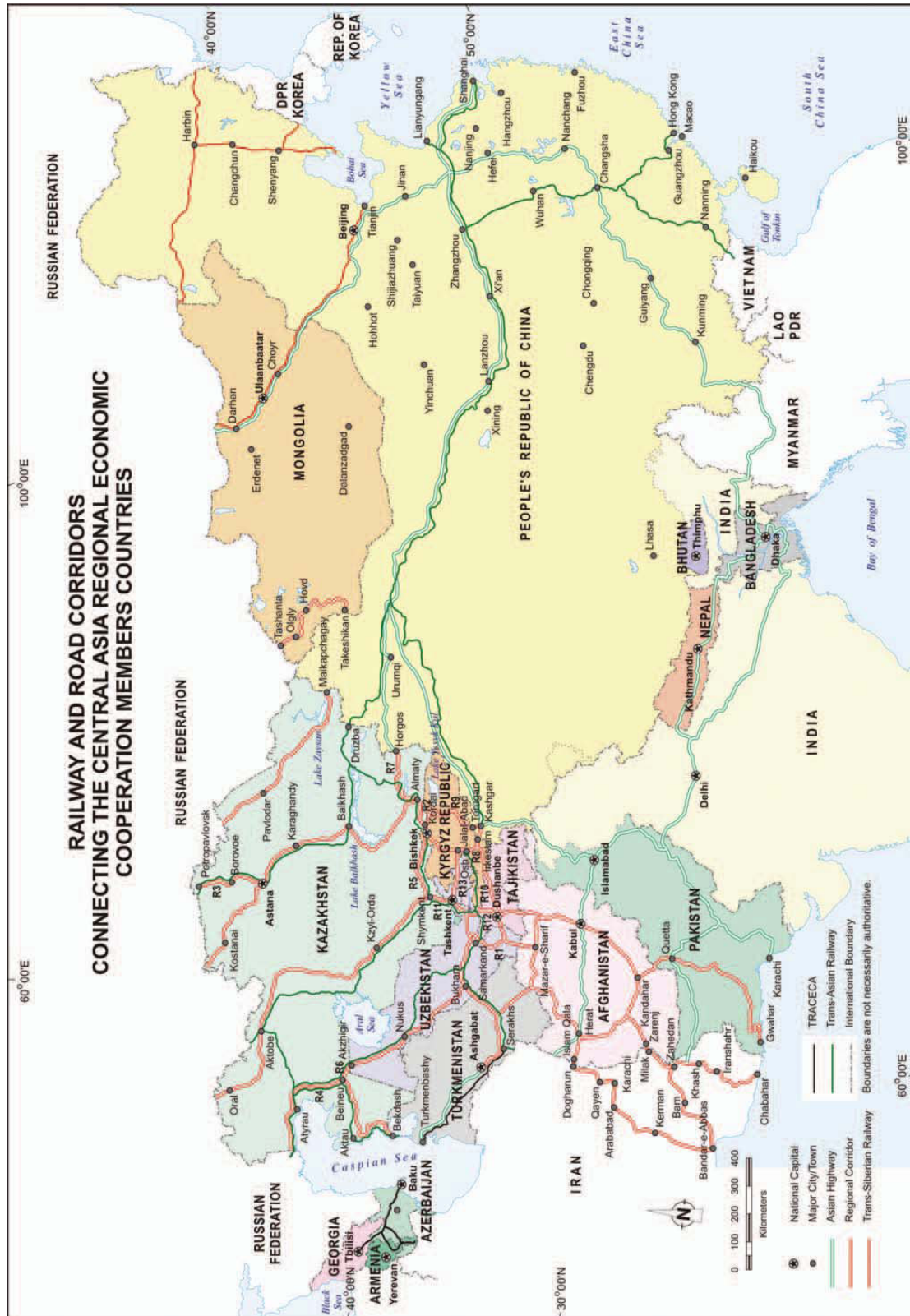
Since, as a result of Soviet policy transportation between these republics constructed such a way that highways and rail roads in the region passed through neighbor territory. Even if connects two town of same republics, especially in Fergana valley. For example, two main Kyrgyz towns connected through Uzbek territory. The road from the Uzbekistan province of Ferghana valley to Tashkent, the Uzbek Capital, was built through the Tajik republic. Gas pipelines and electricity lines from the Uzbek section of the valley into the rest of that republic also ran through Tajikistan; and trade between northern and southern Tajikistan had to cross through Uzbekistan.

Exit roads and railway from Tajikistan run across Uzbekistan. In the winter, when the Anzob Pass is blocked by snow, the only road connection between the north and south of Tajikistan runs across Uzbek territory. Connecting road of Osh-Batken, Kyrgyz towns, runs through the Uzbek exclave of Sokh (Farrant, 2006: 71). The rail way connected south and north Kyrgyzstan passed through Uzbekistan, Tajikistan, and Kazakhstan. The effects of this can be significant. For example, in the Kyrgyzstan transport costs may represent almost 50% of the price of nationally produced goods. The produced price of heating oil is \$50 per ton at the refinery in the south of the country. Bringing it to the north by rail, however, may cost as much as \$27–30 because it must pass through Uzbekistan, Tajikistan, and Kazakhstan. That means oil will sell for about \$90 in the north. For coal, the share of transport costs in the final price is even higher (Asian Development Bank, 2004). Same thing is acceptable for Uzbekistan and Kyrgyzstan. They have to pass through the territory of Kazakhstan to access Russian market. As a result, unsolved border problems and transportation interdependence started to lead to another problem.

Kyrgyzstan and Uzbekistan have to pay due to for transit through Kazakhstan and these countries have proposed to pay off the debt, not hard currency. Uzbekistan used natural gas to pay its rail transit debt. This time, however, Kazakhstan insists on being paid in dollars. When Kazakhstan failed to receive payment in May 1999, it interdicted the movement of passenger trains from Uzbekistan and Kyrgyzstan across its territory until such time as these countries paid off their debts with hard currency. Kyrgyzstan also had a transportation dispute with Uzbekistan, after the latter established extremely high tariffs for the movements of train across its territory” (Rumer, 2000: 12).



Figure 4.1 Map of railway and road crossroads connecting central Asia regional economic cooperation member countries.



With the purpose of restriction on cross-border movement people and goods, to force them and their transportation to use alternative routes to transit Uzbekistan imposed restrictions on cross-border movements of people and transport equipments to restrict imports. Border crossing have been temporarily closed for several month in 1999 Uzbekistan unilaterally closed all. Such actions are often unpredictable and may only be discovered upon arrival at the border (Pomfret 2006: 174). The Tashkent-Samarkand, and Osh-Jalalabad offers a good examples. Tashkent-Samarkand highway, passing through Kazakhstan, was key motor roads used in both domestic and international transportation. During the 11 years of independence Uzbek vehicles pass through Kazakh territory freely. However, in 2002, Uzbekistan closed the Kazakh section of road and tightened rules and procedures for movements of people and vehicles across Kazakh-Uzbek and Kyrgyz-Uzbek borders. As a result Uzbek vehicles started to take a detour around the Kazakh territory, which is longer and in worse condition than the highway (Asian Development Bank 2006: 35). In early 2003 the border with Kyrgyzstan was practically closed to stop Uzbek buyers from taking hard currency out of the country, and tensions between the two states increased. As a result, Uzbekistan's closing its borders caused massive disruption to regional trade. Even, interstate tension increased when people were fired on the border. In July 2003 a Kyrgyz man was killed by Uzbek border guards. A similar situation characterized relations between Uzbekistan and Kazakhstan. This crisis in the relations after December 2002 resulted in the deployment of troops from both countries along the border (Jonson, 2004: 164).

Locating at a great distance from any of the major markets, for the region geographical remoteness from main seaports is a serious disadvantage to the region's participation in international market. According to informed estimates coming from the region, the transportation expenses, on imported goods exceed their original prices by up 60%. Therefore the development of alternative regional transport networks is considered a cornerstone of the national and regional strategies in Central Asia (Bobokulov, 2006: 82). Long transport times are likely to be an obstacle to trade development quite apart from direct transport costs. With transport time between Tashkent and Paris, say, at around 250 hours compared to 25 hours between Paris and

Warsaw, this alone puts Central Asians firms at a substantial competitive disadvantage vis-à-vis Central European firms (Rothert, 2006: 10).

#### **4.5 Other Reasons**

Being fundamental new characteristic social and political system of region corruption has become one of the main obstacles to intra-state and inter-state trade in the Central Asia. It regulates the functioning of the state apparatus, economic activity, and day-to-day lives of population. It has developed such a way that the societies here have come to perceive corruption as a norm of life and it has lost its criminal connotation in public consciousness (Rumer 2005: 7). Despite the fact that there are formally accepted laws or regulations in fact, however, all this sham has become sham. The laws can be simple evaded and ignored if one pays the officials responsible for the functioning of this or that part of the state mechanism. For example, in 2003, a U. S. investment banker was indicted on charges that he made more than 78 million U.S. dollar in illegal payments through Swiss bank accounts to senior Kazakh officials, to win production-sharing agreements for western companies (Mahnovski 2006: 20). If we would take inter regional trade, for example the trade among the CIS countries, there is as well high rate of corruption. For instance, it is estimated that corruption cost at least 2.8 billion a year in the CIS (Ledeneva 2003).

In ordinary life, bribes and payoffs have turned into an obligatory attribute of social relations in the region. The perception of corruption is a very poor. According to Transparency International, all the countries in the region ranked in the bottom of the 145 countries surveyed, as shown in the table.

Table 4.2 Perceptions of Corruption in Central Asian Republics (2004)

Country	Corruption	World Ranking
Kazakhstan	2.2	122
Kyrgyzstan	2.2	122
Tajikistan	2.0	133
Turkmenistan	2.0	133
Uzbekistan	2.3	114

Source: Ledenova, A., 2003, “Commonwealth Independent States”, *Global Corruption Report*, Transparency International, p. 165

The high rate of corruption in the region has generally resulted from the low level wages and arrears. The most common form of corruption typically involve the conditioning of the public good or service on some form of wage (Gleason 2003: 91). In terms of that intra-state and inter-state trade corruption forms have high tendencies to create new one. Simple example, custom officials operate with considerable discretionary power. Sometimes they work with strict rules sometime do not. This is unpredictable. Sometimes they created new type of bureaucratic requirements or standards. For example, direct observation on six occasions indicated that truck and car traffic between Almaty and Bishkek is usually not stopped for Custom inspections rather they were stopped by traffic police or local police (Spechler, 2000). In addition, Central Asian states have complex standards and applications in the cross border points. There are of course, good reasons enforcing standards, but their complexity is many cases resulted in bribes and corruption (Pomfret, 2006: 181).

Other barriers to trade include transit fees beside the costs of dealing with corrupt border officials and local police. For example, road transport costs between Russia and Kyrgyzstan are typically 10–15 percent of total costs, of which only about one-third are fuel costs. The remainder involves different kinds of fees and payments to be made officially and unofficially at various points in transit countries. The main problems arise in connection with transit through Kazakhstan. Many of these barriers are being addressed through an Agreement on Transit that started to be implemented in early 2004. However, some barriers are still in place, including various road taxes and fees imposed by local authorities, as well as harassment by local police,

bureaucratic delays created to extract bribes, and weak capacity in customs administration ( Molnar and Ojala, 2004).

Transporters also complain that axle weight limitations are set differently and are biased against their trucks, and that slight deviations above weight limitations attract draconian penalties, which force them to carry inefficiently small loads (Cuthbertson and Jones, 2000). Tajik drivers complain that current border fees are higher for exports than they are for imports, and that customs regulations are often complex and vague, leaving a great deal of leeway for harassment and bribery (World Bank, 2004). Also, Tajik truck drivers need a visa to enter Uzbekistan, and obtaining or renewing one can be problematic and time-consuming. Since, about 80 percent of Tajikistan's exports must be routed through Uzbekistan, in part because of the topography and in part because Tajikistan's northern and southern rail networks, which carry most of the exports, are not connected.

The objectives of transit should be shortening the travel time, making the date of arrival predictable and preserving the cargo in the same quality as it was dispatched. However, transit through Central Asia or crossing the borders is a complex issue in the region. As a rule a lot of activities take place on the border. Some of these rules imposed by the national railway administrative, worked monopoly, some of them by local administrations. As a result, if freight trains spend 30-40 minutes on the borders in the EU, in Central Asia it takes days and very rarely hours (Molnar, 2003).

Unstable and complex tariff and taxes regulation is could be considered another obstacle to free trade among the Central Asian countries. As a result of transition reforms here formed different and complex tariffs and taxes systems in the region. In Kyrgyzstan and Tajikistan tariffs are fairly low, while Kazakhstan has a rather complex tariff schedule with large number of tariffs bands, for instance. Uzbekistan has a complex and relatively high average tariff rate. For example, in Uzbekistan tariffs, the value added and excise taxes are levied on imports. Imports by individuals are subject to unified tax on imports, the rate of which is 26 % for flour, 40 % for other food products, and 70 % for nonfood products. A serious problem with tariffs in Central Asia is that changes in tariff are rather frequent and unpredictable (Asian Development Bank, 2006).

Moreover, plus to explicit tariffs in some Central Asian states impose other taxes on imports that are not imposed domestically produced goods. Some of them followed protectionist policy. In Uzbekistan, for example, certain commodities, such as construction materials are subject to the value added tax when imported, but exempt for this when produced domestically. Uzbekistan has applied very high duties on automobiles to protect the UzDaewoo joint venture. Kazakhstan suddenly raised duties on intra-Central Asian trade in response to its 1998 crisis (Pomfret, 2006: 174).

In the early 1999, the states of Central Asia began to improve severe restrictions and customs duties on imports. For example, in February 1999, Kazakhstan also temporarily imposed a 200 percent tariff on selected goods from the Kyrgyz Republic and Uzbekistan. This measure was a response to the Russian financial crisis and the sharply devalued ruble that threatened to inundate the region with suddenly cheap Russian goods (Asian Development Bank, 2006). In July same year, Kazakhstan introduced an export restriction on the delivery of fuel oil to Russia and Kyrgyzstan, both of which desperately needed this fuel for the coming harvests. Uzbekistan also established analogous trade barriers against goods from Kazakhstan and Kyrgyzstan. Kyrgyzstan government attributes these actions to the fact that Kyrgyzstan has already become a member of the World Trade Organization (Rumer, 2000: 12).

At the same time, specific, combined, and mixed tariffs are still widespread in Central Asian countries. Kyrgyzstan and Tajikistan apply specific tariffs expressed in EUR, U.S. dollars, or national currency to a volume of some imports expressed. On the other hand, Kazakhstan and Uzbekistan use compound tariffs for some goods applying specific tariffs simultaneously with ad mixed tariffs (Bacalu 2006). Therefore, assessing the overall level of tariffs is complicated by the need to convert these specific and combined tariffs.

The differences in the way of economic development and economic reforms among the Central Asian states was the another main preventing factor of economic unity in the region. For example, Kyrgyzstan introduced the most determined, pro-reform policies in the Central Asian region, perhaps in the entire CIS. Thanks to these efforts Kyrgyzstan pro-reform posture made the country the *Wunderkind* (Gleason,

2003: 81) of the international financial institutions and donors. Kyrgyzstan was the first to introduce a national currency, the first to privatize, and the first country of the CIS to join the World Trade Organization. However these developments negatively effected the development of economic integration in the region. Since other countries in the region have showed more conservative efforts (Rumer and Zhukov, 1998: 125). Thus, differences in the economic structure, institutions, efforts and market had been increasing. Uzbekistan's approach to reforms was also conservative, on the contrary of Kyrgyzstan, and economic transition strategy emphasized establishing self-sufficiency in energy and food grains and creating internally oriented market (Glenson, 2003: 125).

Moreover, stressing economic self sufficiency and state sponsored welfare programs Uzbekistan resisted international organization's advices, which was accepted by Kyrgyzstan and Kazakhstan. Actually, the Uzbek government invited the International Monetary Fund (IMF) into the country in 1994 and accepted its stabilization program, and then abandoned it in 1995 (Olcott, 2005: 22-23). The most important thing in terms of regional integration in international advise was that "the international communities reinforced on country-specific agendas that emphasized local ownership rather than support for overarching regional goals" (Olcott 2005: 24). In their efforts international institutions tried to make countries unique. In addition the leaders on the Central Asian states have emphasized nation-building strategies that maximized competition and minimized cooperation (Glenn, 1999: 141). Although each of these countries faced with similar economic and social problems, the leaders of states feared that his personal position would be damaged if these problems were addressed and solved in correct by other leaders (Olcott, 2005: 24).

Finance related issues were other main problems of integration related institutions as well as Central Asian states. For example, only Kazakhstan and Kyrgyzstan accepted to develop Western-style banking systems that "would facilitate high loan traffic, and only the Kazakhs realized this goal" (Gleanson, 2003: 63). This kind of efforts increased gradually differences between financial systems in the region. For example, towards to the end of 1990s there were some differences in the accounting system, payments system, and reforming the budget system (Craig, 1999:

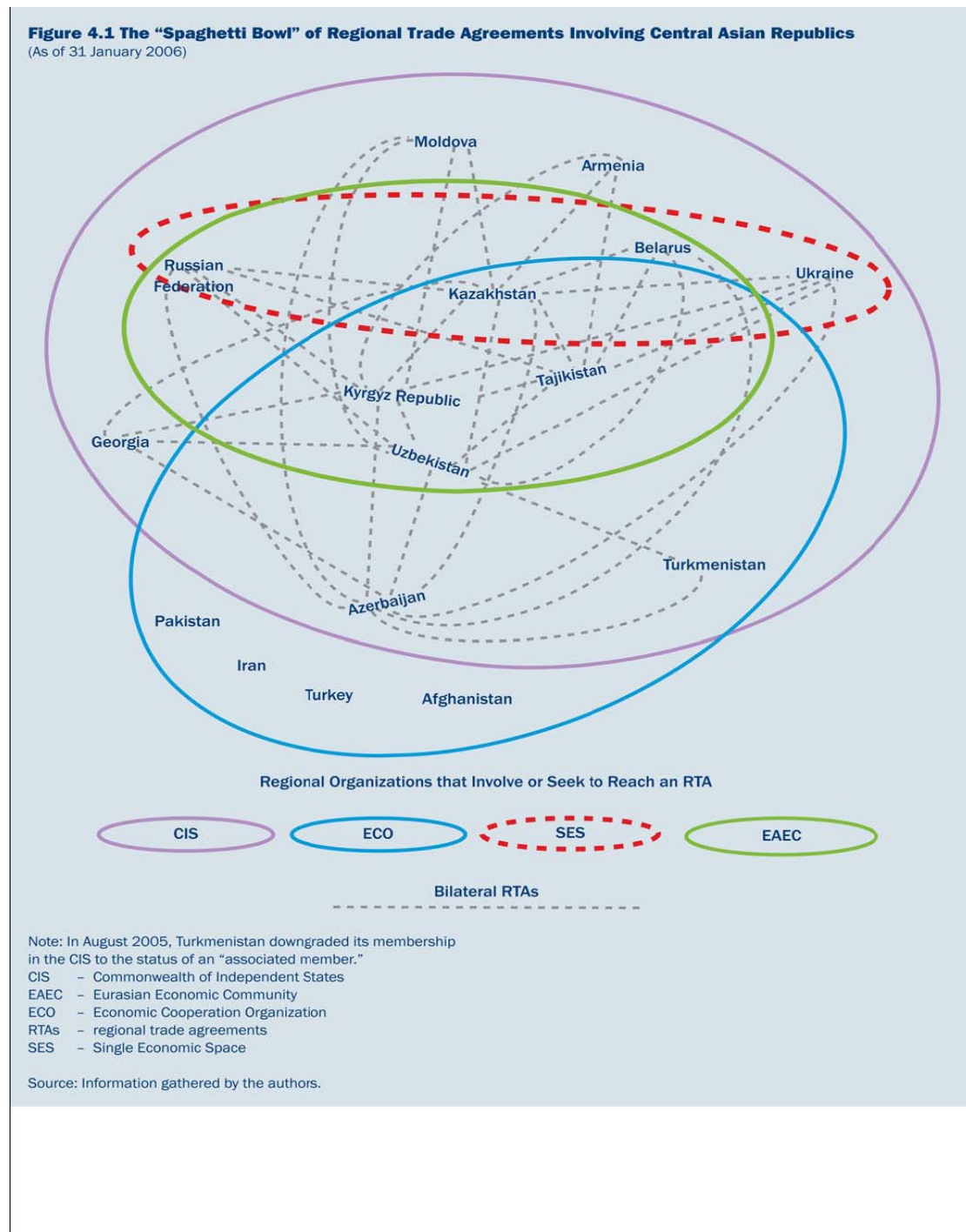
60-69). Another example, “fundamental incompatibility in the differing national system for currency regulation constitutes a obstacles to the development of Uzbekistan’s cooperation with Kazakhstan and Kyrgyzstan” (Rumer and Zhukov, 1998: 119). In spite of pressure of its partners in the Central Asian Union, Uzbekistan categorically refused to sign an agreement on mutual convertibility of national currencies. This also affected foreign investors’ activities in the region negatively. As long as, the member states of the Central Asian Union have substantial differences in currency control, foreign investors forced to resolve problems of inter enterprise payments (Karasar, 2002: 278).

It seems to be like that Central Asia states itself has placed little priority on building regional markets. For example, the Central Asian Cooperation Organization never developed mechanisms concerned action (Olcott, 2005: 227). Similarly, there were some weaknesses of economic integration related institutions in the region. For example, ECO was established as a result of emotional, politic approach of three original countries to Central Asia rather than including common economic goals. For example, Pakistan’s foreign minister M.Sibbiq Khan Kanju declared that “ECO was incomplete without the Central Asian states, the territory of Central Asia has been the main home of all our people and by joining with them we are reaching back to the original homeland of many amongst us” (Anthon, 1996: 40-41).

In addition, the Central Asian Countries have joined several regional organizations that involve bilateral and multilateral agreements. A combination of these multilateral and bilateral agreements has resulted in “spaghetti bowl effect” (ADB, 2006).



Figure 4.2 The “Spaghetti Bowl” of Regional Trade Agreements Involving CAR.



Source: <http://www.adb.org/Documents/Reports/CA-Trade-Policy/chap4.pdf>  
(28.04.2007)

## **CHAPTER 5**

### **Conclusion**

At the beginning of independence Central Asian states showed strong willingness to follow economic cooperation policies with old and new markets. However, the aims of integration and cooperation have become hard to be implemented. The attempts to pursue regional economic cooperation, national economic, social and political reforms simultaneously have produced severe difficulties. It was argued that regional economic cooperation attempts of Central Asian states did not work efficiently due to some reasons and obstacles resulted from transition period. Actually, economic cooperation aimed regional institutions have formed just as a result of political and economic vacuum, formed in the region with the collapse of Soviet Union.

The historical, cultural and linguistic common points of Central Asian have prevented Central Asian economic cooperation rather than to promote it. As we know from history till the 1991 Central Asian nations had been ruled by different empires as a solitary region, result of which Central Asia was owned common ethnical, cultural, and social values in ordinary social life. Moreover, as a result of Soviet economic policy, national economies had been parts of single economic structure of USSR. However, after the independence these common points and structures have created complex and contradictory situation. Since, all of Central Asian states have announced its independence as an independence of titular nation state. In the first day of independence, they faced with necessity of replacement of Soviet ideology and its social and economical model with a new one that could also help them to define their separate “identities”. Therefore, as have seen in the ethnic reasons of inefficiency on economic cooperation, the priorities of policies were focused on strengthening the national identity. In order to strengthen nation identity Central Asian authorities have implemented nation-building policy in such a way that they started to distance themselves from the other states in order to reinforce its own identity. Even, new national symbols and myths have emerged. Although extensive common heritage of

the region seemed difficult to separate what belongs to one nation from what belongs to another, the Central Asian regimes has focused on to differ specific characteristics of one nation from the other nations in the region. By intensifying to differentiate and strengthen their national identity and nation building process at the beginning of independence Central Asian leaders could not have given enough attention and time to regional economic issues.

None of regional economic integration institutions were focused on merely economic issues. Either being one of the aims of organization or changing within the time, economic integration activities could not attract enough and equal priorities from its member. During the formation process of CIS there was a great deal of confusion about the sort of organization that the CIS should become. Ukraine, one of the first members of CIS, saw the CIS as a temporary, transitional organization, while central Asian republics approaches were the CIS as a more enduring structure, showing that it was just instrument of policy, peaceful dissolution of Soviet Union. Although at the beginning economic issues were given priority following years the CIS has become a multipurpose regional organization based on the fairly close cooperation of its members in political, military, economic, social, and cultural spheres. In addition, together with the Tajik civil war and Nagorno Karabag events CIS lost its other fields. Its main focus has become military and political issues. Additionally, several CIS members have started to use temporary import bans against selected neighbors as weapons in a variety of bilateral trade disputes or as emergency measures, even if they have signed multilateral and bilateral trade agreements within the framework of CIS.

Giving the importance to transportation, energy, labor migration and the agro-industrial complex, the EEC was more efficient than others. Since, it defined its activities and responsibilities much more clearly. In addition, being last formed organization among them, EEC benefited from previous experiences. The Central Asian Union, reformed as a CACO following years, was formed as a response to formation of CIS, whereas, GUUAM was founded precisely against Russia. The economic integration aims of both regional organizations stayed under the influence of security issues. The ECO was established as a result of strategical considerations, to which economic dimensions were added. The fundamental aim of ECO was not

economic integration, instead it was geographical strategic locations, regional rich resources of energy and its importance in the regional policy. In addition, there were created contradictory situation among the members. Therefore, the efficiency of organization activities stayed very restricted. In other words, Central Asian economic integration organizations were established from the above, reflecting just interests of politicians. They do not reflected real economic requirements and needs of the region.

There are a number of obstacles and barriers preventing effectiveness of Central Asian countries economic cooperation and integration efforts with old and new markets and as well as within the region. In general similar obstacles and barriers are acceptable for different integration and cooperation institutions. Being result of national economic structures and interests of member countries, and reflecting the interests of ruling elites, the economic policies of each member itself formed the main obstacle to free trade. While, high rate of corruption, lack of infrastructure, unstable border crossing and transit applications, unsolved border issues and transportation, complex tariff and taxes regulations are formed other obstacles to free trade. All the countries in the region have trade focused complex policies and practices. Kazakhstan and Kyrgyzstan have become more pro-reform countries. They have liberalized prices and started privatization of major sectors of the economy including industry, telecommunications and energy by encouraging and supporting regional cooperation. However, Uzbekistan and Turkmenistan followed authoritarian regimes which is the opposite of other Central Asian countries economic policies. Economic policies in Uzbekistan and Turkmenistan in particularly discouraged the establishment of small and medium sized enterprises, thereby preventing the formation not only cooperation in the region bur also formation of traders and business class that would trade with neighboring countries. Among the countries there remains a tendency to view trade as a zero-sum game in which someone wins and someone loses. This tendency even supported by laws and regulations encouraging exports and discouraging imports.

The costs of these obstacles to Central Asian countries could be grouped under four groups. First, they have prevented growth of trade. Second, trade barriers have affected the direction of trade in the region. In particularly, relatively high transport costs and long and unpredictable transit times for international trade shipments to and

from the Central Asia have hindered reorientation of their trade from former old markets to new markets, additional costs for national economy. Third, trade barriers have had impact to the composition of trade. Long and unpredictable transit times have constrained exports lists. The cost is doubled automatically, because export oriented products in the Central Asia based on agricultural one. Fourth, and most important, trade barriers encourage the illegal trade. Faced with high trade tariffs or restrictions traders often resort to illegal ways of conducting trade such as corruption and contraband. As a result, local and international trade in the region goes unrecorded, meaning lost of taxes.

It is important to note that whatever were the dimensions of economic integration in the Central Asia until today, they would face with same problems. Suppose that if there was formed another economic cooperation aimed organization with India, it would also deal with generally same problems. Since, the Central Asian states and ruling elites in the region are not ready to share their authority with supranational bodies. This is the main reason, why Central Asian states faced with “spaghetti bowl” effect. Looking political development of Central Asian states and ruling elites’ political desire we can say that the establishment of efficient supranational institutions in the region far from reality.

Investiveness and unsuccessfulness of these integration concerned institutions lead to new researches around the integrations. As a result of current developments in economy sector in the region and as a result of national economies concerns the new cooperation areas could be seemed in these areas; energy-water resources management and transportation regulation in the region. There are three main reasons why Central Asia needs integration around the energy-water resources and transportation regulation in the region. First, locomotives of national economies in the region these resources could be the main factor of integration. Second, locating between Russia in the north, China in the east, Pakistan and India to the south and Turkey and Iran to the west Central Asia situates in the center of new energy and electricity markets. In addition, it has potential to play role of trade corridor, connecting east and west, north and south Asia, through cooperation in transportation area. Third, it would open Central Asian

states to world market and would increase Central Asian's role in the world economy and policy.

Being locomotives of national economies in the region, petroleum in Kazakhstan, natural gas in Turkmenistan, relatively rich petroleum and natural gas in Uzbekistan, hydroelectricity in Kyrgyzstan and Tajikistan are the main sources of economy. If each country tried to develop itself separately by focusing on its locomotive sector, it could end up in conflict, especially, around the water issues. Since these complementary resources distributed such a way that they located in different country. Thus, the Central Asian countries have to handle economic integration issues focusing on water-energy resources, as well as transportation infrastructure.

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