



# Towards Comprehensive Economic Co-operation between India and Central Asian Republics

## Introduction

At the time of independence around 1990, all the Central Asian Republics (CARs) had middle-income status with a high level of achievement of Millennium Development Goals (MDGs). They did not suffer from widespread income poverty, social deprivation, or gross income inequality. Literacy was nearly universal as was education at primary and secondary levels, and approximately 30 per cent of students went on to enter higher education in the Soviet Union and East Europe. There was no gender discrimination in education. Similarly for health care there was nearly universal free-of-cost coverage for primary health services and free access to tertiary and specialty hospitals, although subject to long waiting periods and often with poor quality. Social protection for the elderly was nearly universal, although modest. Life expectancy at birth was more than 70 for females and about 65 for males in all CARs. There were few, if any, urban slums.

What happened at Independence was simply disastrous. At that time, these countries faced a difficult triple transition: (i) from centrally planned to market-based economies, (ii) from totalitarian communist systems towards pluralist democracies, and (iii) from Soviet republics to sovereign nations. The transition shock resulted in a large-scale loss of employment, income and purchasing power in all CARs. Breakdown of the production and distribution network under Council for Mutual Economic Assistance (CMEA) resulted in the closure of a large number of industrial facilities. Cessation of budgetary support from Moscow led to a near collapse of social sector expenditures. There was hyperinflation, caused by disruption in supplies of necessary goods and loss of control over money supply as CARs switched from the Soviet ruble to independent currencies. There was also migration of

large number of skilled Russians and other nationalities to their home countries which disrupted economic activity in the CARs. Altogether, CARs were plunged into what was one of the worst economic debacles of the twentieth century. During the Great Depression, G-7 suffered a cumulative GDP loss of about 77 per cent spread over a period of six years (1929-36). Japan after the Second World War suffered a cumulative GDP loss of 209 per cent over an 8-year period (1944-53). China in the Great Leap Forward suffered a cumulative GDP loss of 94 per cent over a 4-year period. By contrast, CARs suffered a cumulative GDP loss of 320 per cent over a 12-year period (1990-2002).

Despite some recovery in recent years, CARs are in difficult economic situation and they present a serious challenge to Asia. They are located in the very heart of the continent and political and social disturbances in the region can have adverse effects on the whole continent. On the other hand, a vibrant Central Asia with good connectivity with neighbours can provide an excellent bridge for Asia to Europe and vice versa. As of now, on business as usual scenario, there is a serious risk of economic, political and social deterioration in Kyrgyzstan and Tajikistan with serious risks to the stability of the region. Turkmenistan and Uzbekistan are increasingly under the seize mentality and missing on the opportunities of opening up in trade and investment. Kazakhstan seems to be well-placed to follow a new policy of development grounded in its realities but needs help of the region for a more balanced development. It is in the mutual interest of CARs and the rest of Asia to explore how CARs can become better integrated with Asia and share Asia's resurgence.

This policy brief presents some reflections on how CARs and India can co-operate more effectively.

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## India-Central Asia Links

Central Asia has great historical and cultural ties with successive Indian empires and states beginning with the Indus Valley civilization in the second millennium BC. These exchanges were weakened during the 19th century when the colonial rivalry between the Tsarist Russia and British Empire and the 'Great Game' (1880-1901) for strategic domination and territorial expansion led to separation of areas of influence between two regions. During the cold war era, India had special access to this Soviet region in terms of closer economic, political and cultural relations. In the initial years of independence of the CARs, India could not accelerate its diplomatic moves to meet the challenges in Central Asia. More recently, India is moving closer to CARs with India's inclusion in the Shanghai Cooperation Organization as an observer heralding a new phase. Although India has been late in catching up with action in Central Asia, it is now making up for time lost with proactive diplomacy. It is in the mutual interest of India and CARs to design bolder programmes of economic co-operation. This note argues that India needs to be more active to:

- (a) give intellectual confidence to CARs in developing and implementing their own Eurasian model of development which follows a middle path on both democracy and markets;
- (b) provide financial and technical resources to revive their agriculture, industry and services;
- (c) Improve connectivity and liberalize trade and investment regimes for greater exchange of goods, services and capital.

## Contribution to Development Paradigm

While thinking of development paradigm in CARs, it is useful to have a bit of historical perspective. By and large, the leaders of CARs were not fully convinced of the need for sudden switch to free markets and democracy as were some of their Russian counterparts in the early 1990s. They did not give up their faith in social and economic engineering and in strong leadership. When Soviet Union was dissolved, they looked around the world for different models of development. Fact-finding teams were sent to many east Asian countries such as Korea, Indonesia, Malaysia and China to examine what could be learnt from their experiences regarding political and economic models for development.

However, the force of circumstances did not allow them to experiment with these models. The break-up of Soviet Union and the political upheavals in Russia created a crisis situation where resort to Western assistance became unavoidable. And along with that assistance came the model of democracy and market, even though they were not fully congruent with the local conditions.

The sudden switch to markets and democracy were associated with crises of varying degrees in all CARs and in the decade of 1990s CARs along with other Former Soviet Union (FSU) countries were plunged into what was, as mentioned earlier, probably the worst economic crisis of the 20th century. As and when the circumstances permitted, the CARs have been trying to move toward models more in line with their circumstances. Turkmenistan was the first to move. Uzbekistan soon followed. Then came switch over in Kazakhstan as their growing oil revenues permitted them to implement independent policies. Kyrgyzstan and Tajikistan are still dependent on external resources and despite widespread misgivings are unable to depart fully from the failed doctrines of reforms of the recent past. A lack of consensus on development paradigm is detrimental to co-operation and development within the region and it will be helpful to achieve greater convergence on development paradigm in the region. India can perhaps help in that process.

India is an example of gradual reforms and middle path in terms of the role of state and market. Whether it is liberalization of trade or capital flows or role of financial sector or infrastructure or private sector investment or social protection, India has not subscribed fully to the philosophy represented by the so-called Washington Consensus. Instead it has tuned its policies to its stage of development and local conditions. Many outside observers feeling frustrated by India's measured pace on reforms have been pessimistic about India's prospects. But over time India's approach is proving right and its growth rate is being accelerated. Indian experience can help to increase confidence of CARs in their own way of reforms. This can perhaps be illustrated with reference to financial sector reforms in CARs.

In the wake of hyperinflation in the early 1990s and bank failures in many CARs in the mid-1990s, confidence in financial system is very weak. The degree of monetization is extremely low even in comparison with low-income countries of South Asia. As a consequence of underdeveloped financial systems, lending interest rates are at what may be called 'usury' levels: in 2003 these rates were 21.7 per cent in Kyrgyz Republic, 26.3 per cent in Mongolia, and 16.6 per cent in Tajikistan. In real terms these rates were 17.1 per cent, 20.6 per cent and 6.1 per cent. It is difficult to envisage much private investment with productivity high enough to pay such high real interest rates. A key issue here is restoration of confidence in banking system and that has proven difficult on the basis of private sector initiative alone. An alternative approach may be to set up initially joint ventures between state and private sector (including foreign private sector) with government backing for deposits. Once the confidence is restored, the role of public sector may be reduced. India can provide much technical assistance and perhaps joint ventures for development of financial sector in CARs.

Similar opportunities for learning from India's experience are present in most areas of development, in particular technology development, trade and foreign exchange management, utilization of workers' remittances and partnership between public and private sector for infrastructure development. There should be an active programme for exchange of scholars and development officials between India and CARs to explore these possibilities for intellectual co-operation.

## Helping the Industrial Recovery in CARs

In most of these economies, production of agricultural and/or industrial production remains well below that in 1990. Even in Kazakhstan where over time, GDP has recovered to the 1990 level, production of major commodities remains well below the 1990 level: production of wheat in 2004 was 10 mt as against 16 in 1990; manufacturing index was 10 per cent below even the 1980 level, electricity production was 67 mill. kwh as against 87 in 1990. In Tajikistan, production of coal in 2004 was 68 thousand tonnes as against 475 thousand tonnes in 1990, cotton production 557 thousand tonnes as against 842 in 1990, cement production 194 thousand tonnes as against 1067 in 1990, while the overall manufacturing index was 49 in 2003 as against 100 in 1990. Similar loss of production has been experienced in Uzbekistan in production of coal, cotton, cement and steel. In some of these areas, production capacity might have been irretrievably lost but in some others they may be a potential for rapid recovery. Indian businessmen can be encouraged to explore the possibilities of joint ventures to help in industrial and agricultural recovery in CARs. There are also opportunities for joint ventures in banking, insurance, agriculture, information technology, and the pharmaceutical industry. Multilateral institutions such as the World Bank Group and Asian Development Bank are keen to assist CARs and there may be opportunities for creative mechanisms for trilateral co-operation between CARs, India and multilateral agencies for reviving the industries and agriculture in CARs.

## Increased Trade between India and CARs

At present, CARs account for less than 2 per cent of India's trade. But there is considerable potential for increasing this trade, even though as a share of trade of a large country such as India, it may remain rather small. Central Asia is hungry for a range of goods and services, which India can provide at competitive prices. Both India and Central Asia have economic complementarity in terms of resources, manpower and markets. Certain Indian commodities, for example, tea and drugs, pharmaceuticals and fine chemicals have established a foothold in the Central Asian market. India has to strive hard to increase its exports to Central

Asia in order to maximise mutual benefits through bilateral trade cooperation. This region with a 55 million consumer market has huge potential waiting to be tapped.

Among the potential areas for increased trade and investment are: energy and mining, power generation, telecommunication equipment, healthcare and medical industry, agri-business, tourism, IT sector, food processing and packaging, housing and construction, banking and financial services. In each of these sectors, it will be desirable to field teams of sector experts from India to identify the opportunities and modalities for exploiting the same. In what follows we illustrate these possibilities with reference to five areas.

### *Energy*

With rapidly growing economy, India is emerging as a major importer of energy and diversification of energy supplies is a key component of India's energy security policy. India now imports 50 per cent of its gas and two-thirds of its oil. By the end of the decade oil and gas imports could account for 80 per cent of consumption. Although a new gas discovery along India's east coast will help reduce imports, improved access to Central Asia's energy resources could play an important role in meeting India's energy needs, particularly in the prosperous northern India which is far from the sources of energy in India and could be the entry point for energy imports from Central Asia by land. Apart from oil and gas resources of Kazakhstan, Turkmenistan, and Uzbekistan, the hydro-power in Kyrgyz Republic and Tajikistan could be of great interest to India.

### *IT sector*

CARs have a rich endowment of human resources with strong background in mathematical and engineering sciences which could help in development of IT sector. India has utilized its engineering background to develop a world-class IT sector and can play an important role in developing IT sector in CARs. Kazakhstan Government has expressed keen interest in such co-operation and India will soon be setting up a software park in Almaty, the former capital and commercial hub of Kazakhstan. Kazakh President Nursultan Nazarbayev has, in fact, offered India an "IT-for-oil" deal under which India will help Kazakhstan in IT ventures in return for expanded cooperation in the energy sector.

### *Tourism*

Central Asian splendor of natural and historical beauty provides great scope for tourism from India. Tajikistan and Kyrgyzstan provide tourist spots as attractive as the famed Kashmir region of India, while Uzbekistan is rich in historical sites of great interest to India. Package tourism covering these areas could be popular and cost-effective particularly during the hot summer

seasons in India. Indian tourism industry is also becoming internationally competitive and can build up a profitable network of tourism in CARs.

### *Petrochemical complexes*

Oil and gas rich CARs, in particular Kazakhstan, are keen to maximize value-addition in using their natural resources and want to develop downstream industries which can produce fertilizer, plastics, pharmaceuticals, etc. Private oil and gas companies are neither interested nor competent to help in such broad-based development. India with its vast experience in development of such downstream industries and with enormous demand for these products could be a natural partner to help in maximizing value addition from oil and gas in CARs.

### *Transport and Construction*

As CARs are diversifying their trade and investment patterns, there is an enormous need for developing

new transport routes (roads, railways and airways) and improving connectivity among CARs themselves and also between CARs and South Asia. Many of these infrastructure projects can attract finance from international agencies and Indian firms can provide competitive bids for such projects. Indian construction companies can also play an active role in providing cost-effective services for construction sector which is booming in some CARs such as Kazakhstan.

### **Conclusion**

The above are but some examples of areas where India and CARs can co-operate for mutual benefit. There is an urgent need to develop an institutional mechanism for promoting such broad-based co-operation. The old approach of forming FTAs is inadequate for that purpose. Comprehensive Economic Co-operation Agreement (CECA), as initiated between India and Singapore, could be a better model for promoting co-operation between India and CARs.

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Research and Information System  
for Developing Countries

Core IV-B, Fourth Floor  
India Habitat Centre  
Lodhi Road, New Delhi-110 003, India.  
Ph. 91-11-24682177-80  
Fax: 91-11-24682173-74-75  
Email: [dgoffice@ris.org.in](mailto:dgoffice@ris.org.in)  
Websites: <http://www.ris.org.in>  
<http://www.newasiaforum.org>