

The Problem of Exporting Energy Resources from Central Asia

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In terms of its reserves of hydrocarbon raw materials, Central Asia is one of the richest regions of the world. Thus, the proven reserves of oil in three Central Asian republics—Kazakhstan, Turkmenistan, and Uzbekistan—amount to approximately 20 billion barrels, and the reserves of natural gas constitute 10 trillion cubic meters.

In the Soviet era, the bulk of the oil and natural gas produced in this region was shipped northward to Russia (through the gas pipeline network “Central Asia-Center” and the oil pipeline “Atyrau-Samara”). However, once the Central Asian states acquired independence, they immediately faced an acute question about the choice of new routes to transport their raw materials. The urgency of this question resulted from the fact that, above all, the states of the region wanted to reduce their shipping dependence on Russia.

It is no secret that Russia, exploiting its monopolistic right to transport oil and natural gas from Central Asia, rather often used this fact to put political pressure on the states in this region and to impose its own conditions during price negotiations. As a result, it was extremely urgent that the newly independent states of Central Asia make an effort to gain direct access to prospective markets in Europe, South Asia, Southeast Asia, and the Far East. Moreover, this would also provide a powerful stimulus for them to increase their production of hydrocarbons and help attract foreign investment to the region.

With the construction of new transportation routes, the states of Central Asia also sought to stabilize the political situation in the region. The transformation of these states into leading exporters of oil and natural gas would create a situation where the importers from South Asia and Europe would have an

interest in strengthening stability and in maintaining guaranteed access to the hydrocarbon resources of Kazakhstan, Uzbekistan, and Turkmenistan.

However, the available information shows that the success of the Central Asian countries in this question has hitherto been quite modest. The only breakthrough during all the years that have passed since the breakup of the USSR was the pipeline Korpjeje-Kurt Kui, which transports the natural gas of Turkmenistan to the northern regions of Iran.

At the same time, it should be pointed out that the gradual increase of American influence in the region (which followed immediately after the events of 11 September 2001 and the beginning of the antiterrorist campaign in Afghanistan) has led to an increase of Western interest in the energy resources of Central Asia. As a consequence, there has been the activation of plans to involve Kazakhstan in the Baku-Ceyhan pipeline project and a renewed interest in the idea of constructing a natural gas pipeline from Turkmenistan to Pakistan (through the territory of Afghanistan). These two projects probably represent the greatest interest today (from both an economic and geopolitical perspective). Hence this article will concentrate on providing a comprehensive examination of these two projects, with some attention to the other potential avenues of export.

The Problem of Exporting Oil from Kazakhstan

A Short Prehistory of the Question

In the course of several years, the Baku-Ceyhan project has already been considered as one of the proposed routes for shipping Kazakh oil to world markets and, above all, the European market. The question of Kazakhstan's participation in this project was first raised at a summit of the Organization for Security and Cooperation in Europe (OSCE) in Istanbul in 1999, and since then it has been repeatedly discussed at meetings of the Kazakh leaders with American and Turkish officials.

It is of course no accident that the participants and sponsors of the Baku-Ceyhan project should turn their attention to Kazakhstan. In the opinion of a great many experts, this interest was dictated by the fact that the reserves of

Azerbaijani oil are clearly not sufficient to keep the pipeline filled over the long term; the guaranteed inclusion of Kazakhstan's oil would not only increase the profitability of the pipeline, but also raise its attractiveness in the eyes of international petroleum producing companies.

As far as Kazakhstan is concerned, its position on this question has been characterized by an extreme degree of uncertainty. On the one hand, the Kazakh leadership signed an aide-mémoire in Astana in 2000, whereby it affirmed its intention to participate in the Baku-Ceyhan project. On the other hand, it has constantly issued "fuzzy" declarations about its support for the idea of a "multiplicity of routes" to transport Kazakh oil and about the economic expediency of a pipeline running in the direction of Iran.

Naturally, such a situation could not continue for long, and by the middle of 2000 information began to appear that the Baku-Ceyhan project could be profitable without the participation of Kazakh oil. Specifically, the calculations by the firm British Petroleum claimed that the oil pipeline Baku-Ceyhan could yield a profit of 24.5 percent even without Kazakhstan's participation.

However, it seems that such declarations had a substantial political undercurrent and sought to push Kazakhstan to take more active steps in this matter. Unquestionably, despite all the declarations by the experts of British Petroleum, Kazakhstan's oil is nonetheless very important in order to realize the Baku-Ceyhan project as quickly as possible and to enhance its profitability. This fact was clearly confirmed by the visit of Stephen Mann (the U.S. special envoy to the Caucasus) to Astana in the middle of March 2002; his objective was to secure the agreement of President N. Nazarbaev to ship Kazakh oil through the oil pipeline Baku-Ceyhan.

At the same time, in evaluating Astana's evasive policy in recent years with respect to participation in the Baku-Ceyhan project, it should be noted that this posture was no accident. Rather, it seems to be based on a recognition of the economic and political difficulties that Kazakhstan would encounter in the event it decides to use the Trans-Caucasus pipeline to transport its oil.

Here we shall attempt to analyze all the possible factors that, in our view, could either lead to delays in shipping Kazakh oil through the Baku-Ceyhan pipeline or prevent its participation altogether.

Will the Baku-Ceyhan Pipeline Receive Kazakh Oil?

Among the problems that Kazakhstan could face in the near term, one should note its capacity to provide the Baku-Ceyhan pipeline with the requisite volume of oil. In 2001, Kazakhstan produced 40 million tons of oil. Moreover, under current shipping facilities, it can export up to 47.5 million tons of oil per year. Above all, this includes the pipeline of the Caspian Pipeline Consortium (which can handle up to 28 million tons of oil per year), the Atyrau-Samara pipeline (15 million tons per year), and transport by sea to Makhachkala (4.5 million tons per year). Kazakhstan has the prospect of raising its transportation potential, through the Baku-Ceyhan pipeline, to 67 million tons per year. It can also increase shipping through the Makhachkala route to 7.5 million tons per year.

Altogether, therefore, Kazakhstan could increase its export potential to 90 million tons per year. If one takes into account the declarations of Kazakh officials about plans to increase oil production by 5 million tons per year, one can assume that by 2005 Kazan will produce up to 60 million tons of oil.¹ Taking into account the parallel increase in domestic oil consumption, at the point when the Kashagan oil fields go into production in 2005, Kazakhstan can presumably export no more than 40 to 45 tons of oil. These volumes mean that it can fill no more than half of the existing export routes. The existing capacities entirely suffice to handle the oil from the Kashagan oil fields until the years 2011-2012, when production there will reach the level of 1 million barrels per day (with a total output of 57.6 million tons per year).

Without question, the fact that Kazakhstan already has pipelines and shipping routes can have a serious impact on the decision of the Kazakh leadership whether their country should join the Baku-Ceyhan project or, at least, defer this step for several more years.

Transportation and Ecological Problems

Another important problem involves the task of shipping Kazakh oil to the coast of Azerbaijan. That can be done only through two means: either by constructing a trans-Caspian pipeline or by relying upon oil tankers. Both variants, however, have several substantial drawbacks. Above all, laying a pipeline on the bottom of the Caspian Sea is highly problematic, given the fact that its territorial

¹"V 2004 godu Kazakhstan nameren dobyt' 55 mln. tonn nefi - ministr ekonomiki i trgovli," *Kazakhstan Today*, 28 March 2002.

status in international law has not yet been regulated. In addition, the region has an elevated level of seismic activity (with a shifting seabed and the presence of underwater geysers).

Protests by ecologists could play a significant role in preventing the construction of a trans-Caspian oil pipeline and the use of large-scale oil tankers. That is because any shipping accident can lead to an ecological catastrophe in the Caspian Sea. In principle, the world today is already a witness to this catastrophe. Thus, in the year 2000 alone, approximately 30,000 Caspian seals perished, followed by another 8,000 in 2001.² As a result of the intensive oil drilling in Atyrau Oblast of Kazakhstan, during the last decade morality in this region has risen by 39.4 percent and fertility has fallen by 30.3 percent. In 2001, of every 4,200 infants born, 756 had a pathology. In the opinion of specialists, one of the principal causes of the crisis situation in this oblast is the 6 million tons of caked sulfur that is stored in the open air at Tengiz.³

What Are the Security Guarantees?

If one considers the possibility of exporting Kazakh oil through the Baku-Ceyhan pipeline, it is also necessary to raise the question of the security of shipping through this route. It is obvious that the oil pipeline must pass through the territories of several states that already are hotbeds of serious instability. The first of these is the region of Nagornyi Karabakh: despite all the efforts by the Azerbaijani and the Armenian sides as well as international mediators, it has still not been possible to resolve this dispute. This conflict has the potential of destabilizing the situation in a region that lies directly on the route of the proposed export of Kazakh oil.

The situation in Georgia is also a source of considerable concern, since it has several areas with an unstable political situation. These include, above all, Abkhazia and Southern Ossetia. And although the appearance of American military advisors in Georgia has had a favorable impact in terms of improving the security of the Baku-Ceyhan pipeline, the potential threat of a deterioration in Georgian-South Ossetian and Georgian-Abkhazian relations nevertheless remains rather high.

The key element in determining the security of the shipping route for

²"Thousands of Dead Seals Washed Ashore in Azerbaijan in 2001, Expert Says," *Caspian News Agency*, 1 April 2002.

³M. D. Diarova, "Nef' ili zdorov'e," *Caspinfo - Biulleten'* 72 (1/15 April 2002).

Kazakh oil over the Baku-Ceyhan pipeline is Turkey's neighbor, Iraq.

The efforts by the United States, within the framework of its international antiterrorist operation, to have a radical influence on the political situation in Iraq and to change the regime of Saddam Hussein with a more democratic government, in the foreseeable future can have a quite negative influence on the situation in those Turkish areas adjacent to Iraq. The uniqueness of the domestic political situation in Iraq consists in the fact that there is essentially no democratic opposition to the ruling regime of Saddam Hussein in the Western conception of that word. Oppositionist forces consist essentially of religious organizations, such as Ansar al-Islam, the Supreme Council for the Islamic Revolution in Iraq, and ethnic movements and parties such as the "National Party of the Turkmen of Iraq," "the Kurdistan Democratic Party," and the "Patriotic Union of Kurdistan."

Given all this, the removal of Saddam Hussein from power can only precipitate chaos in the country and lead to its possible breakup into several pseudo-state formations. It can also contribute to the spread of instability to the contiguous governments. In this respect, an Iraqi Kurdistan is particularly dangerous, for it could become the long-term rear base for Turkish Kurds in waging their own struggle to create a Turkish Kurdistan separate from Turkey. Naturally, this growth of instability in the southern areas of Turkey will also serve to undermine the interest of foreign investors in participating in the Baku-Ceyhan project.

To What Degree Does Kazakh Oil Require Additional Access to the European Market?

Apart from these problems, Kazakhstan also faces the question of the expediency of obtaining, beyond the existing transportation routes, yet another line of access to the European oil market.

Without question, the European market is highly attractive for the states that export oil: it is second only to the United States as a net importer of oil (approximately 8.5 million barrels per day) and has a high level of purchasing power. These factors, in turn, have generated rather stiff competition on the European market from the various oil exporters, who are all seeking to ensconce themselves as firmly as possible. Apparently, the competitive struggle on the

European market in the next few years will become even more intense. There are several reasons for this.

First, by 2010, it is predicted that there will be a sharp growth in the production of oil in the states of the Persian Gulf (from approximately 19 to 30 million barrels per day) and in Russia (which may increase its exports from the current level of 4.7 million barrels per day to 6.0 million barrels). Given all this, one can say, with a high degree of confidence, that these countries will endeavor to direct the largest possible amount of their oil to the market of the European Union.

Second, the rate of growth in the volume of oil imports by the European states is relatively low. As the current dynamics for the growth of oil consumption on the West European market shows, by 2010 the European countries will import approximately 11 million barrels of oil per day—i.e., an increase of no more than 2.0 to 2.5 million barrels per day. In principle, that is comparable with the growth on the American market and, by several magnitudes, less than the growth of aggregate oil imports by Chinese, Indian, and Japanese markets.

Third, it is necessary to pay attention to the possible appearance, in the near future, of powerful competition to Kazakh oil and to the Baku-Ceyhan pipeline from oil production in Iraq.

In the event that the United States and its allies succeed, in the shortest possible span of time, in resolving the Iraqi problem and do not permit the instability to spread to the territories of contiguous states, one can expect a full-scale return of Iraqi oil to world markets.

As is well known, Iraq has the second largest proven reserves of oil in the world (surpassed only by Saudi Arabia), the reserves being estimated at 112 billion barrels. Currently, this country delivers about 2.5 million barrels of oil per day (because of the sanctions). In the event the sanctions are lifted, Bagdad could quickly raise production to 3.5 million barrels per day. As many experts point out, the Iraqi oil production industry, with the support of international companies, can increase the daily output to 6 million barrels per day, with some estimates running as high as 8 million barrels per day.

The blueprints for the main routes to transport Iraqi oil to world markets also show that, in some points, they can clash with the interests of the Baku-Ceyhan pipeline.

In particular, the oil pipeline Kirkuk-Ceyhan (with a load capacity of 1.1 to 1.6 billion barrels per day), in the event it goes into operation, can pose the most serious competition with Baku-Ceyhan in the struggle for the European market.

Iraqi oil, in addition, can be delivered to the European market through the oil pipeline Iraq-Saudi Arabia (IPSA-2), which was closed in 1990. This pipeline can enable the delivery of up to 1.65 million barrels per day to the Saudi shore on the Red Sea; the oil can then be shipped by tankers through the Suez Canal to countries bordering on the Mediterranean Sea.

Moreover, if Iraq returns to the world oil market as a full-scale producer, another serious negative consequence for Kazakh oil would be a further intensification of price competition.

Iraq, given that its economy is in extremely severe straits, is now experiencing an acute need for financial resources, but in the short term it can obtain these only from the sale of oil. In this regard, it is entirely logical to expect that Iraq is endeavoring not only to send the maximum possible volume of oil to the world market (in violation of its OPEC quota), but to demand from the members of this organization an increase in its share of oil exports. Here one must take into account the fact that Iraq, taking advantage of the low production costs of its oil (no more than 2 dollars per barrel) will agree to sell its oil more cheaply than the other exporters. As a result, it could come to pass that the cheap Iraqi oil will drive much of the oil from Kazakhstan and Russia off the European market.

Given the foregoing, one can conclude that, in principle, it would not be entirely expedient and rational to direct the bulk of Kazakhstan's oil exports through the several oil pipelines that are oriented mainly toward Mediterranean markets—where, in fact, one can expect to encounter intense competition in the future. This not only would deprive Kazakhstan's oil policy of flexibility, but also make it directly dependent on the situation in the European oil market. It would be much more logical to diversify the channels for delivering oil to Europe through the existing pipeline systems and, in addition, to attempt to gain access to the markets of the Far East, South Asia, and Southeast Asia.

Possible Avenues for Oil Exports from Kazakhstan

The diversification of routes to deliver Kazakhstan's oil to Europe consist of the following.

1. *The oil pipeline Atyrau-Samara to Al'met'evsk, then through the Baltic Pipeline System to the Russian port of Primorsk or the Latvian Ventspils.*

The advantage of this route lies in the fact that it can give Kazakhstan's exporters the capacity to react more flexibly and effectively to changes in the situation on the European market and, if need be, to direct their oil both to the markets of northern Europe and to the Mediterranean (along the traditional Atyrau-Samara-Lisichansk-Odessa route).

2. *The project for an oil pipeline Druzhba-Adria.*

This pipeline has a projected capacity of 15 million tons of Russian and Kazakh oil per year and would follow the route of Samara-Omisalj (a Croatian port on the Adriatic Sea)-Genoa. This pipeline would make it possible to transport Kazakh oil over a route that not only bypasses the Bosphorus Strait, but also one that can even reach the North American market.

3. *The Russian-Bulgarian-Greek project of Novorossiisk-Burgas-Alexandroupolis.*

This pipeline would have a projected capacity of 35 million tons of oil per year.

4. *The route of Odessa-Brody-Gdansk.*

This pipeline is designed to deliver 40 million tons of Caspian oil per year to Germany and the countries of Eastern Europe.

As for the question of Kazakhstan's access to the regions of the Far East, South Asia, and Southeast Asia, it should be pointed out that this is an extremely urgent matter for Astana, since a prompt resolution of this issue would give

Kazakhstan's oil guaranteed access to the highly promising and ever-growing Asian markets. The fact that these markets hold great potential for Kazakh oil is evident from an analysis of the oil consumption of the three largest Asian net-importers of oil: Japan, China, and India. At present, the scale of the net oil imports amounts to approximately 5.5 million barrels per day for Japan, 1.6 million barrels per day for China, and 1.1 million barrels per day for India. Notwithstanding the fact that, in terms of the volume of oil purchased abroad, each of these markets today is significantly smaller than the European or American markets, these countries exhibit an impressive rate of growth in their consumption of hydrocarbon raw materials. For example, in China and India this growth is about 7 to 8 percent per annum. Taking all this into account, experts predict that by 2010 oil imports will amount to approximately 7 million barrels of oil per day for Japan (an increase of 1.5 million barrels), 5 million barrels per day for China (an increase of 3.4 million barrels per day), and 3 million barrels per day for India (an increase of 2 million barrels per day). The total increase in the aggregate volume of oil imports to these three countries, compared to their current consumption, will amount to approximately an additional 7 million barrels per day. These figures show that the Asian-Pacific region will become, in the very near future, the largest and most attractive market for oil exporters.

The delivery of Kazakh oil to the Asian markets can be realized through several possible routes:

1. By the construction of an oil pipeline in China and up to the shore of the Sea of Japan. At present, there are three oil pipeline projects: Western Kazakhstan-China, Angask-Dasin, and Angarsk-Nakhodka.

The Western Kazakhstan-China line (Atyrau-Kenkiak-Kumkol'-Atasu-Druzhba). This pipeline would have a length of 2,800 km.; it foresees the delivery of a minimum of 20 million tons of Kazakh oil per year from the Caspian oil fields to the Chinese border.

The Angarsk-Dasin pipeline. This project is intended to transport 30 million tons of oil from eastern Siberia to the northern regions of China.

The Angarsk-Nakhodka project. This pipeline would have a length of 3,765 km and a capacity of 50 million tons. It is proposed that this pipeline deliver Russian oil to the Asian-Pacific region and, possibly, to North America.

2. Through Iran, using the principle of “oil exchange.” Under this plan, when oil from Kazakhstan is delivered to Iranian petroleum refineries in the northern part of that country, Iran would in exchange ship its own oil from terminals in the Persian Gulf. There is also a pipeline project: from Kazakhstan, via Turkmenistan, to the Iranian shore on the Persian Gulf.
3. A pipeline following the route of Kazakhstan-Turkmenistan-Afghanistan-Pakistan.

Realization of the Iranian and Afghanistan routes, at the present time, is exceedingly problematic—for a number of political reasons, including the instability in Afghanistan and the complicated tenor of Iranian-American relations. At the same time, it is impossible to discount the probability that, already in the very near future, Kazakhstan will acquire the opportunity to export its oil to Asian markets—at a volume ranging between 800,000 and 1,000,000 barrels per day—through one of the above routes.

Thus, in judging the prospects for the export of Kazakh oil through the oil pipeline Baku-Ceyhan, it is necessary to note that they are quite uncertain—given the numerous political and economic obstacles that stand in the way. At the same time, it should be emphasized that there are a number of reasons that would induce Kazakhstan to decide that it should in this project. These include the so-called “Great Political Game” between the United States and Russia (to gain dominance over the region of the Caucasus and Central Asia) and also the desire of the West to obtain an additional route to transport Caspian oil to European and American markets (as insurance in the event of a possible deterioration in Russian-Kazakh relations).

At the same time, in considering the question of delivering Kazakh oil through the Baku-Ceyhan pipeline, one must always take into account another important factor: the position of the Kazakh leadership itself. In my opinion, much will depend on the position of Astana itself takes in determining which direction Kazakh oil will flow in the coming years.

Problems in the Transport of Natural Gas

The most ambitious and controversial project for shipping Central Asian and, especially, Turkmen natural gas is the proposal to construct a pipeline running along this route: Turkmenistan-Afghanistan-Pakistan-India. It would have a projected capacity of 20 billion cubic meters of Turkmen natural gas per year and would run from the gas fields at Davlatabad through Afghan territory to consumers in Pakistan and India. However, the appearance of the radical Islamic movement “Taliban” in Afghanistan in 1994 precipitated a new wave of armed conflict in that country and prevented the realization of this plan.

Recent events associated with the international antiterrorist campaign in Afghanistan and the overthrow of the Taliban have had the effect of reviving plans to build the Turkmen-Afghan-Pakistan gas pipeline. This was clearly demonstrated by the meeting of the head of the provisional Afghan administration, Hamid Karzai, with President Saparmurad Niiazov of Turkmenistan and President Pervez Musharrarf of Pakistan; in the course of their discussions, they repeatedly touched on questions pertaining to the delivery of Turkmenistan’s natural gas to Pakistan through the territory of Afghanistan.

The renewal of dialogue on this question, without doubt, is a good sign and bears witness to the fact that, in the very near future, the main participants in the project (Turkmenistan, Afghanistan, and Pakistan) can probably conclude an agreement on the construction of the gas pipeline.

At the same time, in analyzing the prospects for realizing this project, one must note that a political consensus of Ashgabad, Kabul, and Islamabad is by no means a guarantee for its complete success. As the available data show, at the present time there are a number reasons why it would be impossible to realize the above plan.

Regional Instability

With respect to political instability, the problem of resolving the Afghan crisis (which has gone on for many years) ranks as among the most serious obstacles to realizing the pipeline project.

The departure of the Taliban from the Afghan domestic political arena

has created an extremely complicated and unpredictable situation in Afghanistan. On the one hand, processes to restore statehood are gaining momentum in the country; on the other hand, the return of many ethnic and tribal leaders to active political life in Afghanistan (together with the strengthening of their positions in areas where they traditionally held sway) has contributed to the emergence of a potentially unstable situation in the country. Today the official government in Kabul holds only nominal control over the situation in many provinces of the country. If one looks at the proposed route for the gas pipeline from Turkmenistan, it will obviously have to pass through the following volatile regions:

- *Herat province*: this area is under the control of the forces of the governor, Ismail Khan, who is known for conducting a policy that is largely independent of the central Afghan authorities;
- *Nimruz, Helmand, and Kandahar provinces*: these territories are carved up into zones of influence under the domination of numerous tribal and criminal authorities, who are constantly engaged in an armed struggle with each other.

In addition, one should also mention that of late the relations between the population of northern Afghanistan and the Pashtun population in the south have sharply deteriorated. This is due to the fact that the Pashtuns living in the north have been subjected to persecution by the national minorities of Afghanistan. This fact has its own deep historic roots and, in the future, will certainly remain one of the potential sources of instability.

At the same time, one of the key factors in this crisis derives from the fact that Afghanistan still has a large number of people who are adherents of the Taliban and al Qaeda. The position of these two forces, despite a series of major defeats, nonetheless continues to be quite strong. The majority of the members of these radical Islamist groups have only dissolved into the midst of the peaceful Afghan population; they are simply biding their time until they can again launch active armed attacks on the central Afghan authorities and the forces of the international coalition that supports them. Naturally, in the event the gas pipeline is actually constructed, they will not forego so attractive an opportunity to conduct a large-scale assault.

Among the most acute problems that face the sponsors of the gas pipeline project, one should also mention the question of "Pashtunistan." In essence, the problem derives from the fact that, after two bloody Anglo-Afghan wars, in 1893 the king of Afghanistan (Abdurahman-Khan) and Great Britain signed an agreement creating the "Durand Line," which assigned lands populated by the tribes of the eastern Pashtun to British rule. However, the leaders of the eastern Pashtun have never recognized this agreement, and that led to continuous Anglo-Pashtun wars.

After the formation of Pakistan, Afghanistan raised demands that the agreement be annulled and that an independent state of Pashtunistan be established on the territory of the British Northwestern border province. That, in turn, became the grounds for a sharp deterioration in Pakistani-Afghan relations that very nearly ended in an armed conflict in 1955.

The fact that today the Afghani and Pakistani officials demonstratively are *not* discussing the problem of Pashtunistan does not at all mean that the issue has ceased to exist or has lost its urgency. An analysis of the peculiarities of Afghan domestic political life shows that, as the situation in the country becomes normalized, nationalist tendencies will gain momentum in the upper echelons of power. And the main thrust of such sentiments is the question of returning the territories that are populated by Pashtun, but now formally within the state of Pakistan.

Even the Taliban movement, which had rather close ties with Islamabad, not only spurned an agreement to recognize the North West Frontier Province (populated by Pashtun), the northern regions of the province of Balochistan, and bands of "Free Pashtun Tribes" as the property of Pakistan, but in August 2001 sent its own delegation to the territorial agency Mohmand, which belongs to the Federally Administered Tribal Areas. Its purpose was to explain to the local Pashtun population that their land is part of Afghanistan.⁴

It is probable that, with time, the Pashtunistan issue can again become a stumbling block in Afghan-Pakistani relations and will create significant difficulties for realization of the project to construct a gas pipeline. This is made all the more urgent by the fact that the validity of the Anglo-Afghan Treaty on the "Durand Line" expired in 1993. As a result, in terms of strict legal terms, the lands

⁴Dr. G. Rauf Roashan, "The Unholy Durand Line; Buffering the Buffer" (11 August 2001, Institute for Afghan Studies).

populated by the eastern Pashtun tribes now belong to no one. Sooner or later, this problem is bound to make itself felt.

The proposed gas pipeline can also expect to encounter a myriad of political problems on the territory of Pakistan. Above all, this includes the problem of separatism, which exists in the Pakistan province of Baluchistan, the northern part of which would be crossed by the Turkmenistan-Afghanistan-Pakistan pipeline.

The Baluchi tribes that populate this province have already, for many years, waged a struggle to gain broad autonomy for their province of Baluchistan and even to achieve its total separation from Pakistan. Moreover, this struggle has often assumed the character of an armed conflict. The target of attacks are primarily state installations, such as the pipeline from the largest Pakistan gas field at Sui. Given the high degree of politicization for a gas pipeline from Turkmenistan, one can say with a high degree of confidence that it may well become the goal of various acts of sabotage.

Moreover, the general situation in Pakistan as a whole is a cause of considerable concern. The presence of a large number of nationalistic and radical Islamist groups in the country poses a substantial threat to the stability of Pakistan. The seizure of the city of Chilas by Islamists at the end of 2001, the murder of the American journalist Daniel Pearle, the bombing of the bus with French citizens—all these events provide ample grounds for concern.

Given the foregoing, it is obvious that potential foreign sponsors who construct a gas pipeline from Turkmenistan to Pakistan face a very high level of political risk. Until the situation in the region is fully stabilized and the leadership in Afghanistan and Pakistan can give firm guarantees for the security of investors, one should simply forget about the gas pipeline for an indeterminate period of time.

Just how great is Pakistan's demand for natural gas from Turkmenistan? Apart from political difficulties, various economic problems can also have a significant influence on the rates at which the project is realized. These include the economic rationality of importing Turkmen gas to Pakistan, competition from the gas pipelines of Iran and Qatar, and so forth.

At the present time, there are two diametrically opposed views with

respect to the problem of the efficacy of importing natural gas from Central Asia to Pakistan. The two views rely upon different assessments of the rates of growth of consumption of natural gas in Pakistan and its production in Central Asia.

According to one of these, demand on the Pakistan market for natural gas will increase 50 percent by the year 2006. Moreover, with each passing year, there will be an increasing difference between the growth of consumption of natural gas and the capacity of Pakistani gas fields to supply the necessary amount of this raw material.

Table 6-1
Increases in the Shortage of Natural Gas in Pakistan

Year	Growth of demand (billions of cubic feet per day)	Growth of production (billions of cubic feet per day)	Difference (billions of cubic feet per day)
2000	2.7*	2.2	0.5
2005	3.7	3.1	0.6
2010	4.2	3.4	0.8
2015	4.6	3.6	1.0

* 1 cubic foot equals 0.028 cubic meters

Source: Sui Southern Gas Company Limited ("Gas supply, demand gap rising," 12 March 2002)

Simultaneous with the increase in demand on the domestic market in Pakistan, there will be growth in the share of natural gas in the aggregate volume of consumption of energy sources (from a current level of 47 percent to 58 percent by the year 2010). All this will occur against a background that forecasts a substantial decrease by the year 2010 in the production of natural gas at the main gas fields in the province of Baluchistan.

According to another scenario, the above calculations regarding such rapid rates of growth in the consumption of natural gas in Pakistan are somewhat inflated. This view is based on the fact that the economy of Pakistan, in the course

of the past five years, has been in a profound crisis that was provoked by the economic sanctions imposed by Washington in 1998 (for testing nuclear weapons) and annulled only in the year 2001. A further negative factor influencing the economy of Pakistan is the prolonged drought, the substantial payments to service the foreign debt, and the burdensome expenditures on the armed forces (which consume approximately 17 percent of the country's annual budget).

Those who oppose the import of natural gas from Turkmenistan advance one further argument: in recent years, as a result of exploratory geological work, a whole series of large gas fields have been discovered in Pakistan (for example, Khairpur, Qadirpur, Uch, Sawan, and Zamzama). According to the estimates of experts, development of these gas fields would enable Pakistan to increase its production of natural gas by more than 10 billion cubic meters per year, a volume that would largely satisfy domestic demand for many years to come.

Turkmen Gas and the Rising Competition on Asian Markets

In addition to the murky situation with respect to the future demand on the Pakistani market for imported natural gas, the gas pipeline project from Turkmenistan faces another rather complex problem: the competition of natural gas from Iran and Qatar.

Iran, which has the world's second largest reserves of natural gas (15 percent of world reserves), in recent years has sharply increased its production of this hydrocarbon. Thus, in the fiscal year 2001-2002 (calculated in Iran from 21 March of each year), production reached 120 billion cubic meters. In the thinking of the Iranian leadership, natural gas should become the country's largest source of hard currency in the coming years and thereby reduce its excessive dependence on the export of oil. In this regard, Iran actively develops plans to find markets for this raw material and regards Pakistan as one of the potential consumers of its natural gas.

In turn, it is more attractive for Pakistan to purchase natural gas from Iran than from Turkmenistan.

First and foremost, the Iranian gas fields are relatively close to the Pakistani border and have significant reserves of natural gas. Moreover, the traditional good relations between Pakistan and Iran make the delivery of Iranian

natural gas entirely safe—which is not something one can say about plans to deliver this hydrocarbon across the territory of Afghanistan.

Second, the most probable competitor for Turkmenistan on the Pakistani market is Qatar. The latter has concluded a preliminary agreement with Pakistan to accelerate the construction of an underwater gas pipeline from the Qatar gas field “North Field” to the Pakistan shore—the so-called “Delphin Project.” The planned gas pipeline would cost 3 billion dollars and deliver 29 million cubic meters of natural gas per day (10.5 billion cubic meters per year).⁵

The presence of such powerful competitors could negate all the efforts by Turkmenistan to establish itself on the natural gas market of Pakistan.

Nevertheless, in assessing the situation on the Asian market of natural gas consumers, it should be noted that the likelihood of shipping significant volumes of Turkmen gas along the Turkmenistan-Afghanistan-Pakistan pipeline would increase substantially in the event that the gas is delivered to India or to countries in the Pacific-Asian region.

The Indian market for natural gas is one of the fastest growing in the world. In the period from 1995 to 2000 the consumption of natural gas in India rose from 17 to 34 billion cubic meters per year, and by 2003 will climb to 64 billion cubic meters. It is forecast that, by 2020, the rate of growth in the consumption of natural gas in India will be 6.5 to 7.0 percent per year. Taking into account the fact that the proven reserves of natural gas in India amount to just 650 billion cubic meters, at the current rate of production India will turn into a net importer of oil in eight to ten years.

As a result, India will undoubtedly be interested in arranging the delivery of natural gas from Turkmenistan. However, if one takes into account the fact that the pipeline will traverse the territory of Pakistan (with which India has exceedingly acute disagreements over the Kashmir issue), the realization of such a pipeline will probably be deferred for an indeterminate period.

In examining the question of delivering Turkmen gas to India, it is also necessary to note that Turkmenistan possibly has no more than ten years in which to realize this project. That suggestion is based on the fact that several other countries are seeking to claim a role as the main supplier of natural gas on the Indian market, including Iran, Bangladesh, Qatar, Oman, and others.

⁵*Kommersant*, 19 February 2002.

Iran and Bangladesh plan to deliver their natural gas to India through pipelines. That is particularly disadvantageous for Turkmenistan, since such pipeline deliveries presuppose, in the majority of cases, the signing of long-term agreements with terms ranging from fifteen to thirty years.

The Iranian project includes plans to construct a 2,000-km. underwater gas pipeline across the bottom of the Arabian Sea and thus bypass the territory of Pakistan. The Italian companies Snamprogetti and Saipem have already signed a contract to conduct a study of the projects's technical and economic feasibility.⁶

For its part, Bangladesh intends to deliver its own natural gas from the gas fields at Bibiyana to the New Deli region. The length of the gas pipeline is 1,350 km., with construction costs of 900 million dollars. The operator of the project, it is assumed, will be the American company Unocal.⁷

It is expected that Qatar, Oman, and Indonesia will become the largest suppliers of liquefied gas to India. Specifically, Qatar alone can supply up to 7.5 million tons of liquefied gas. A clear sign that India intends to begin importing liquefied gas can be found in its plans to construct twelve special liquefied natural gas (LNG) terminals.⁸ And although the realization of many projects has now been halted, the growing demand in India for natural gas will undoubtedly contribute to the re-activation of work in this direction.

In addition to India, the natural gas of Turkmenistan might also be delivered in liquefied form to the most promising world markets in the countries of the Far East, East Asia, and Southeast Asia. However, that would require the construction of expensive gas-to-liquid (GTL) plants in Pakistan as well as the acquisition of LNG tankers to deliver the liquefied gas to Asian consumers.

Moreover, on the Asian markets the Turkmen gas can again expect to encounter stiff competition from the traditional suppliers of liquefied natural gas (viz., Qatar, Malaysia, and Indonesia) as well as from some potential new ones (in particular, countries in the Persian Gulf).

As an indication of the seriousness of the efforts being made by these countries to preserve their markets in the Asian-Pacific region one could cite their plans to increase the export of liquefied natural gas. In particular, Qatar signed an agreement with the company Sasol (Republic of South Africa) to construct a GTL plan with a capacity of 34,000 barrels per day. Iran has also signed a contract with

⁶See www.Iranmania.com, 18.04.2002

⁷USA Energy Administration, 2002.

⁸USA Energy Administration, 2002.

the Anglo-Dutch firm Shell, the South African company MouGas, and the Norwegian firm Statoil to prepare a technical and economic feasibility study for the construct of two GTL plants with a capacity of 70,000 barrels per day.⁹ As for Malaysia, in the near future it will complete work to modernize the world's largest LNG complex at Bintulu (Sarawak); it will be able to produce 23 million metric tons of liquefied gas per year.¹⁰

As the above data show, arranging the delivery of Turkmenistan's natural gas to southern markets at the present time is exceedingly problematic. Nevertheless, to say that Turkmenistan has no chance whatsoever of gaining entre to the Asian markets would be false. As recent events have shown, the situation in the region of Central Asia and Afghanistan is beginning to undergo a fundamental transformation as a result of the increased interest of the world community in Central Asian energy resources and in questions of regional security. In this respect, one cannot preclude the possibility that, as a result of political and economic circumstances, the natural gas of Turkmenistan might become the favorite in the emerging struggle for the Pakistani and Indian markets.

The Western Direction

Is there a chance that the Turkmen gas can be shipped westward? Along with the Pakistani route, there are also several projects to export Turkmen gas to Turkey and then onward to Europe. In the first instance this includes the Trans-Caspian pipeline and the Turkmenistan-Iran-Turkey pipeline.

The Trans-Caspian pipeline provides for the delivery of approximately 16 billion cubic meters of natural gas per year from Turkmenistan, passing over the bottom of the Caspian Sea and then through Azerbaijan and Georgia on to Turkey. At present, however, it is impossible to realize this project for two reasons. Most important, one must note the rather strained relations between Baku and Ashgabad over their conflicting claims of ownership to a number of disputed oilfields in the Caspian Sea. A second factor is the competition from Azerbaijani gas (from the gas fields at Shah Deniz (which has estimated reserves of 700 billion cubic meters of natural gas and 300 million tons of gas condensate). Given the strong competition on the Turkish and European markets, Baku will hardly be interested to help arrange the large-scale delivery of Turkmen gas, especially since it has plans to

⁹See www.iranmania.com, 19.04.2002.

¹⁰USA Energy Administration 2002.

increase steadily its own production and exports from the natural gas fields at Shah Deniz.

Table 6-2
Exports of Azerbaijani Gas to Turkey

Year	Volume of Exports to Turkey (Billions of Cubic Meters)
2004	4-5
2008	10
2010	16
2015	30-32

Source: P. Vasil'ev, "Turtsiia ne mozhet opravdat' nadezhdy kaspiskikh proizvoditelei gaza" (*RusEnergy*, 26.12.2000).

As for the export of Turkmen gas to Europe across Iranian territory, this option again runs into the problem of the competitive struggle for the markets of Turkey and the countries in the European Union. Iran, like the other suppliers of natural gas to the Turkish and European markets, has no interest in seeing the appearance of a new competitor in the form of Turkmenistan. If Iran gains access to the markets of Turkey and the European Union, that would naturally be a principal stimulus to develop its own natural gas industry. As a result, in my opinion, the maximum that Turkmenistan can expect to obtain in the near term is an increase in its gas exports to the Iranian domestic market and perhaps to Armenia. Nevertheless, it must be pointed out that the rates of gas consumption in Iran are quite impressive.

In particular, in 2001 the Iranian domestic market consumed 185 million cubic meters of natural gas per day. It is predicted that, by the year 2005, as a result of the realization of a gasification program in the country, this indicator will rise to 320 million cubic meters per day.¹¹ Without question, such rates of growth will substantially contribute to the constant increase in the volumes of Turkmen gas being exported to Iran.

¹¹"Iran's Domestic Gas Consumption 185 Million Cubic Meters a Day," IRNA (Iranian Republic News Agency), 06.09.2001.

The Northern Direction and the Eurasian Gas Alliance

In examining the problem of exporting the natural gas of Turkmenistan to foreign markets, one cannot ignore the northern (i.e., Russia) direction. Turkmenistan today exports a total of 50 billion cubic meters of natural gas per year through the “Central Asia–Center” pipeline (with 40 billion cubic meters going to Ukraine and an additional 10 billion cubic meters to the Russian gas company Itera). As an analysis of the tendencies prevalent on the Russian and European gas markets shows, the northern direction has every chance of claiming, in the near future, the top priority for the Turkmen exporters of natural gas.

Of the especially important reasons that could push Turkmenistan to increase its gas exports in a northerly direction, one should note the rather complicated situation that has developed in recent years with respect to the Russian fuel and energy complex.

Above all, this concerns the exhaustion of existing gas fields, especially those in Western Siberia, where the average level of exhaustion has reached 60 percent. In recent years, the gas fields that are in the later stages of exploitation (and have declining output) account for up to 85 percent of all Russian natural gas.¹²

All this, to a large degree, explains the steady tendency for the volume of natural gas production by the monopolist “Gazprom” to decline. This can have a negative impact on its capacity to preserve its role as the main supplier of natural gas to Europe, especially under conditions characterized by a constant rise in competition from European, Asian, and African exporters.

The deterioration in the general situation in the Russian gas industry occurs amidst what the Russian company Unified Energy System (EES being its Russian abbreviation) estimates to be a 4-percent per annum growth in energy consumption in the country. The whole difficulty at the present time lies in the fact that natural gas accounts for 50 percent of the output of the Russian electric power industry—the highest indicator anywhere in the world. A reduction in the volume of gas deliveries to the electric power stations would lead to a prolonged energy crisis. The first symptoms of this are already apparent. In particular, according to some data, Gazprom cannot deliver more than 30 billion cubic meters of natural gas to the Unified Energy System in 2002.¹³

¹²R. Orlov, “Ugrozy energeticheskogo krizisa,” *Ekonomicheskie strategii*, Winter 2001, p. 55.

¹³Ibid., p. 55.

If such tendencies in the fuel and energy complex persist (and that is expected to be the case), then by 2020 Russia—according to some estimates—the shortage of natural gas in the country can run to as much as 200 to 300 billion cubic meters.

To avert such a crisis situation, Russia needs to attract significant investments to develop new gas fields and to stimulate the activity of independent Russian producers of natural gas. Today the latter have capacities that allow them to increase production of natural gas to 150 billion cubic meters per year.

Nevertheless, the fastest possible realization of this plan will only be possible if there is a liberalization of the domestic gas market and if independent producers gain access to export pipelines. At the present time, however, that appears to be highly problematic.

In addition to the above, Russia also possesses an alternative—viz., it can increase the delivery of natural gas from Turkmenistan. On the Russian market, however, Turkmen gas can expect to encounter several problems of a competitive character.

The point is that the situation on the Central Asian market of natural gas producers is radically different today from what it was at the beginning of the 1990s. If then Turkmenistan was the main player on the regional gas market, today it is gradually encountering competition from the other states of Central Asia.

In particular, Uzbekistan is undertaking active measures to expand its production of natural gas. That is reflected in a decree that President Islam Karimov issued in 2000: “On Measures to Attract Foreign Direct Investments in the Exploration and Extraction of Oil and Natural Gas.” In addition, Uzbekistan has begun to expand its own network of export pipelines. In particular, in early 2002 the gasmen of Turkmenistan, together with the Russian company Itera, began to construct the new gas pipeline of Gazli-Kagan, which has a capacity of 30 million cubic meters of natural gas per day (that is, 10 to 11 billion cubic meters per year). The new pipeline will link the Ustiurt and Bukhara-Khivin oil and gas regions with the export pipelines of “Bukhara-Urals” and “Central Asia-Center.” There are also plans to use this gas pipeline to transport natural gas from the Kandym group of gas fields (Kashkadarya Oblast), which have an estimated 250

billion cubic meters of natural gas and 10 million tons of liquid hydrocarbons.¹⁴ All this will make it possible to increase, within the next few years, the aggregate export potential to 16 to 18 billion cubic meters of natural gas. Taking into account the geographic location of Uzbekistan, it should be noted that it can pose rather serious competition for Turkmenistan in both the northern and southern directions.

In recent years Kazakhstan has also begun to give close scrutiny to the development of its own natural gas industry. According to the government conception for development in the country's gas industry, the production of natural gas in Kazakhstan by 2015 should rise to approximately 45-50 billion cubic meters per year.¹⁵ Moreover, Kazakhstan plans to export approximately 35 billion cubic meters of gas.¹⁶ Given the territorial proximity of Kazakhstan to Russia, one can easily predict that a large part of the Kazakh gas exports will go in a northerly direction, thereby becoming a direct competitor to the natural gas from Turkmenistan.

The anticipated growth in the production of natural gas in Turkmenistan, Uzbekistan, and Kazakhstan could create, within the next few years, a rather complicated situation on the Central Asian gas market, as the producers face serious problems of gaining access to external sales markets. The urgency of this problem will increase still further in the event there are delays in the construction of the gas pipeline Turkmenistan-Afghanistan-Pakistan-India. In that case, the northern route will gain the highest priority for all the Central Asian suppliers of natural gas.

A direct result of all this will probably be the appearance of intense competition for the right of access to the gas pipeline, price wars, and a consequent upsurge of tension among the states involved. To avert the emergence of such a situation, the Central Asian suppliers of natural gas and their main partner, Russia, would find it expedient to create some kind of economic organization, within the framework of which they could resolve the most acute questions associated with the export of hydrocarbon raw materials. Such an organization might be that which Russian President V. V. Putin proposed—that is, “a Eurasian Gas Alliance.” However, there are several obstacles to the establishment of such an organization.

¹⁴See www.UzReport.com, 17.01.2002.

¹⁵V. Luk'ianchikov, “Kazakhstan raschityvet pokryt' defitsit gaza, nazrevaiushchii v Rossii,” *Petroleum* (Kazakhstan).

¹⁶“Kazakhstan Eyes Key Gas Role in Central Asia,” Reuters, 16.02.2002.

Above all, this includes the persistent fear of the Central Asian states that Russia would use this alliance for its own political purposes. If Russia is really interested in the formation of such an association, then it will have to dispel these fears.

A significant acceleration in the process of unifying all the natural gas suppliers in post-Soviet space could be Russia's decision to do two things: first, grant the states of Central Asia a quota on gas exports to the European market and, second, provide a guarantee that the new organization will not limit the rights of its members to cooperate with third parties in the matter of producing and exporting natural gas.

In my view, the formation of a real gas union will have a beneficial effect for all its participants. It will allow them, under conditions of the unfolding globalization throughout the world, to become more actively integrated into world economic processes. This will also create the necessary grounds for the emergence of a unified economic space on the territory of the former USSR and will have the prospect of serving as one of the most important links in the formation of a common Eurasian market.

Conclusions

In summing up my analysis of the problems of shipping Central Asian energy resources to world markets, I would like to point out that, at the present time, Kazakhstan and Turkmenistan have still not found an attractive alternative to the Russian direction. At the same time, those processes which in recent years are unfolding in Russia attest to a gradual transformation of its approach to Central Asia. Today, the criterion of economic benefits has increasingly become the cornerstone of Russian policy. In the event that these processes really become irreversible, Russia can become a very promising and reliable partner of the Central Asian states in the sphere of producing and transporting energy resources.

At the same time, cooperation with Russia does not at all preclude Central Asian states from seeking to find alternative export routes. To the contrary: these efforts should be intensified, since the presence of several pipelines will make their export policy more balanced. However, one must also pay heed to economic expediency, not just some geopolitical motives—which can lead to significant financial losses. Oil and natural gas are strategically important goods for

the states of Central Asia; while these reserves are still large, they must be used with maximum advantage. That will make it possible for the Central Asian states to become full-fledged participants in the global energy market and to provide a stimulus for the further development of their economies.

The Agriculture of Azerbaijan: Condition, Problems, and Prospects

Ingilab Akhmedov

It has so happened that the world associates Azerbaijan, a small country that recently gained its independence, only with oil. And any interest in Azerbaijan, in one way or the other, is linked to its large reserves of hydrocarbons.

However, Azerbaijan has astonishingly favorable and diversified climatic conditions as well as equally rich traditions of agricultural production.

A careful analysis of the condition of the economy and the tempo of reform graphically demonstrates the enormous potential of the agrarian sector in Azerbaijan, but as yet it is not fully realized.

The branch structure of the economy of Azerbaijan today provides eloquent proof of the ten-year period of transformation processes in the country and the logical consequence of the path taken. A special place here belongs to agriculture. An examination of the place and role of the agricultural sector in the economy will make it possible, after moving beyond the current situation, to give a more profound evaluation of what is transpiring.

Today the proportion of agricultural production in the structure of the gross domestic product (GDP) amounts to 15.7 percent. By comparison, the share of industry as a whole is 35.5 percent of the GDP, and transportation and communications account for another 12.3 percent. Despite the relatively high rates of growth in agriculture in recent years (with the rate of growth of agricultural production in 2001 being 11.1 percent), as a whole the share of this branch in the total volume of production—which traditionally had been a leading branch in the economy of the republic—is undeservedly small. Moreover, this sector participates less and less in both the establishment of macroeconomic equilibrium and in the investment process. If the dynamics of the rate of growth in agriculture in recent

years demonstrate a clear tendency to increase, the volume of investments in this sector in no way corresponds to its potential and clearly lags behind the rate of increase in the volume of investments in the economy as a whole. The most dangerous thing is that in recent years there has been a clearly visible contraction in the volume of investment in the agrarian sector and indeed a catastrophic decline in this indicator. If in 1995 the proportion of investments in agriculture in the total volume of investments in the economy amounted to 1.9 percent, in 2001 this indicator was equal to just 0.7 percent. Of course, such a situation is mainly due to the incomparably greater volume of increase of investments in oil. However, that is not the only cause of the decline in the rate of investment in the agrarian sector.

Table 7-1
Dynamics of Investment in Agriculture
(billions of manat)

Indicator	1995	1996	1997	1998	1999	2000	2001
Total investments (billions of manat)	1140	3222	4942	5512	4643	4684	5649
Investment in agriculture (billions of manat)	216	483	198	343	548	323	417
Rate of growth of investments in agriculture (percent)		223.17	40.90	173.27	160.09	58.90	128.80
Proportion of total investment in agriculture (percent)	1.9	1.5	0.4	0.6	1.2	0.7	0.7

Source: Goskomstat Azerbaidzhana, 2000 and 2001.

During the Soviet period, the agriculture of Azerbaijan developed in accordance with the principles of the all-union division of labor and the socialist distribution of productive forces. The boundless Soviet market created an enormous demand for heat-loving agricultural crops (early vegetables, tea, citrus, fruits, and much else) that could only be cultivated in the several southern republics of the Soviet Union. To a large degree, it was precisely because of the special character of the Soviet market (which was relatively closed to the external world and which enabled the producer to feel carefree, given the absence of external competition) that the agricultural producers of Azerbaijan were placed in conditions favorable for themselves. It was no accident that immediately after the breakup of the Soviet Union and the proclamation of a transition to a market economy, the Azerbaijani peasant encountered conditions which he found extremely difficult and unusual.

In the Soviet period, the agriculture of Azerbaijan was not only an “all-union garden,” but also constituted an inextricable part of the processing and food complexes that had been created in the republic. Vertical integration, which was intensified in the periods of the creation of the agro-industrial complex, was implemented rather well in the republic. A careful analysis of the internal structure shows that agriculture at that time functioned primarily to supply the foodstuff complex of the country. Based on the inter-branch balance of Azerbaijan in 1987, one can show that, of the total volume of the gross output of agriculture, 35 percent went to the food industry, 27 percent for personal consumption, and only 6.6 percent for export. In general, the food industry accounted for 17.1 percent of the gross social product of Azerbaijan, while agriculture itself represented only 15.2 percent.

As is evident from these statistics, the agriculture of Azerbaijan in the Soviet period was not—contrary to the assertions of some—a typically raw-material exporter to other republics of the USSR. On the contrary, it was rather well integrated into the republic’s own agro-industrial complex, with the goal of creating the final industrial product in Azerbaijan itself. In this vertically-integrated structure, the processing industry played a dominant role. It was directly responsible for generating high rates of growth in the production of agricultural products.

It seems to me that this is the key to explaining the further development of the agricultural branch and the reform in this branch.

The Beginning of Reform

Immediately after the proclamation of independence in 1991, Azerbaijan faced the very acute problems of defining property ownership of land and establishing an adequate form of agricultural organization in the agrarian sector under conditions of a market economy.

Unfortunately, in contrast to many other former socialist republics, it was practically impossible for Azerbaijan to resolve these questions during the first years of the reform. The war with Armenia and the extremely unstable social and political situation in the first half of the 1990s, in essence, deprived the government of the opportunity to become fundamentally engaged in agricultural reform. The sole positive step taken by the government during his period was the adoption of a number of basic legislative statutes that served to determine ownership of land and the forms of economic organization under the new conditions.

Legislation

The laws of Azerbaijan in the sphere of agriculture are quite comprehensive and progressive. Practically all the spheres of the agrarian sectors are treated in the legislation and in accordance with the values that are generally accepted throughout the world. Moreover, according to some statutes, Azerbaijan has left behind many post-Soviet countries and confidently leads in the democratization of relations in agriculture.

Thus, according to the Land Code (already adopted in 1991, that is, immediately after the republic proclaimed its independence), land is transferred to citizens gratis, with equal treatment accorded to private, collective, and state ownership of land. The law provides for the existence of all forms of economic organization, including collective farms, state farms, peasant (farmer) households,

associations, and so forth. Moreover, land plots are not to be sold as property to foreigners; nor is land to be returned to former owners (as restitution). Peasants who are given ownership of land plots gratis for commodity production have the right to sell the land, but only after a five-year term has elapsed.

The “Law on Peasant (Farmer) Households” exempted peasants from paying any tax on land during the first three years. This statute also provides for the use of the land plot as a security deposit to back the grant of preferential credits; the term for extinguishing these loans commences six months after receipt of the credit.

The “Law on the Foundations of Agrarian Reform” provides for a complex of measures of state protection for the agrarian sector. These include measures to stimulate investment, to implement targeted state programs, to support the proportionality of prices between the industrial and agricultural sectors, to establish differentiation in credits and taxation, to protect domestic commodity producers from the influence of foreign markets, and much else.

In addition, during various years of the transformation process, the country adopted and implemented laws “on the leasing of land,” “on land reform,” “on land cadastres,” “on grain,” and so forth.

As is readily apparent, in general Azerbaijan has adopted sufficient laws to provide a legal foundation for the agrarian sector. This legislation is necessary for the effective development of agriculture and for reforms in this sphere.

However, as practice has shown, conditions in the agrarian sector are quite difficult. One gains the impression that the adopted laws and ongoing processes in this sphere are not coordinated with each other.

During the first years of the reforms, in the early 1990s, the agriculture of Azerbaijan was dealt irreparable harm. Immediately after the liberalization of economic relations (and the proclamation of freedom with respect to prices, credit, banking, and hard currency), there commenced—as indeed should have been anticipated—a hyperinflationary spiral. That inflation dealt a blow that struck the agricultural producer more than anyone else. The dismantling of collective and state farms, to a large degree, proceeded in a spontaneous fashion; the government created nothing to replace them.

Moreover, rather than protect the extremely vulnerable market of the

country against an inundation of agricultural products from neighboring countries, the government did everything possible to encourage a flood of cheap and often low-quality goods, primarily from Iran. One must take into account the fact that, geographically, Azerbaijan is situated on the transit juncture of large suppliers of foodstuffs, such as Russia, Iran, and Turkey. Hence, simultaneous with the proclamation of a liberalization of foreign economic relations, it was also necessary to activate the protectionist levers of the state to shield the domestic agriculture producers, who as yet were only weakly developed. In practice, however, nothing was done. As a result, the deliveries of foreign citrus, fruits, and vegetables mercilessly devastated the plantations of the local competitors in southern Azerbaijan.

Later, when the fantastic damage from this virtually criminal policy finally received its proper assessment, the government at last placed a barrier in the way and sharply reduced the import of food products into the country. Unfortunately, all this came too late. The market had been totally destroyed; the purchasing-power of the main mass of the population had fallen precipitously during this period.

Systematic, targeted work in the sphere of reforming agriculture did not commence until the stabilization of the social and political situation in the middle of the 1990s.

Negative Creation

Beginning in 1996, the state began to distribute land plots gratis to peasants, but until now it has essentially not gone any further.

The main stumbling block in the question of effective reform processes in agriculture is the fact that the state, conceptually, has not yet determined the position it should occupy and what should be the priorities of reform in this sphere. Is it necessary to give preference to small peasant households, supporting them only by the requisite state regulation? Or should the government make the creation of large agro-holdings its top priority? Or, finally, should the government itself investment in the agricultural branch and become an active “player” along with the private sector? All these questions are rather complicated; for the

government to take the sole correct decision, it was necessary—after announcing private ownership of land—to take the initiative into its own hands and to organize practical work. The government, by contrast, has almost totally excluded itself from this sphere and has left the peasant alone to face his problems by himself.

After the breakup of the Soviet system, the village—which, during socialism, was largely left under the care of the city—found itself in very difficult straits. The village suffered a collapse of its technical, chemical, and processing system as well as its financial infrastructure; nothing was offered to replace all this. As a result, a great imbalance emerged in the village: an enormous number of idle labor (one must remember that Azerbaijan had always been characterized by a surfeit of labor resources) and the virtual absence of demand for this labor.

As a result, in many respects the current level of development in the agrarian sector and the general condition of the village in Azerbaijan are being shaped by inertia and are a logical result of the chaotic development of the situation in this sphere. If, in the beginning of the reform process, agricultural was regarded as a real alternative to the one-sided development of the economy in Azerbaijan and as an effective means to help diversify the economy, that is today regarded as almost impossible.

During the reform years, the tendency of development in agriculture was such that this branch was transformed from a producer of commodity production into an enclave for the self-sufficiency of the population. Simultaneously, there also transpired an extensification of agricultural labor and universalization of the production of agricultural products at the cost of specialization (for which the republic had once been famous).

Statistics show that, in the course of the 1990s, there has been a clear downward trend in the main commodities, such as cotton, grapes, vegetables, citrus, tea, etc.

In lieu of these, there has been a growth in the production of goods that above all bear the character of ensuring the self-sufficiency of the peasants themselves. Typical in this sense is the production of grain, which reached a volume of 2,016,600 tons in 2001 (compared to an average output of about 100,000 tons in the mid-1990s). The same can be said about the products of animal husbandry, which is almost entirely consumed within the boundaries of the

republic and produces no items at all for export. Likewise, the production of cotton, compared with the early 1990s, has fallen sixfold and now amounts to just 83,700 tons.

Table 6-2
Production of Individual Agricultural Products
(thousands of tons)

Product	1990	1994	1995	1996	1997	1998	1999	2000	2001
Grain	1,413.0	1,039.0	921.4	1,018.8	1,127.1	947.1	1,093.4	1,540.0	2,016.6
Cotton	542.9	283.7	274.1	274.4	124.6	112.6	96.8	91.5	83.7
Tobacco	53.3	10.0	8.5	11.2	15.1	15.2	8.0	15.1	12.8
Potatoes	185.0	150.3	155.5	214.0	223.4	310.0	391.2	468.9	605.3
Vegetables	856.2	482.9	424.1	570.0	495.4	502.6	632.6	780.8	916.0
Fruits	320.0	323.5	324.4	321.2	330.9	385.5	394.4	260.8	492.3
Grapes	1,196.0	313.8	308.7	274.9	145.3	144.0	112.5	76.8	68.0
Tea	30.7	19.4	9.4	3.0	1.6	0.9	2.7	1.1	1.4

Source: *Goskomstat Azerbaidzhana, 2000 g., 2001 (ianvar'-dekabr')*.

Under these conditions, the well-known indicators of growth in agriculture do not entirely reflect the situation. What is required is a detailed qualitative analysis.

The complexity of evaluating the real situation lies in the fact that the official statistics about the quality of gross output from agriculture does not methodologically make an accurate count of the entire volume of production, since a substantial part of this is intended for consumption by the producer himself. This fact indirectly confirms that today the majority of agricultural production consists of products that the peasants have produced on their own land plots. Incidentally, the State Statistical Committee regards this category as “personal auxiliary farming” (a term used to describe production on household garden plots).

Table 6-3
Agriculture According to Categories of Producer Types
(in percent)

Producer Category	Production Share	1995	1996	1997	1998	1999	2000
All categories	Total	100.0	100.0	100.0	100.0	100.0	100.0
	Crops	58.6	58.6	60.0	60.9	60.9	58.2
	Animal husbandry	41.4	41.4	40.0	39.1	39.1	41.8
Agricultural enterprise	Total	32.7	32.7	25.9	6.7	6.7	4.2
	Crops	83.3	83.3	83.3	91.8	91.8	99.1
	Animal husbandry	16.7	16.7	16.7	8.2	8.3	0.9
Individual auxiliary plots	Total	67.3	67.3	74.1	93.3	93.3	
	Crops	46.6	46.6	50.5	58.7	58.7	
	Animal husbandry	53.4	53.4	49.5	41.3	41.3	

Source: Goskomstat Azerbaizhdana 2000-2001.

Thus, it is not difficult to discern the extremely unsatisfactory situation in agriculture when, in essence, the entire population of Azerbaijan (in one degree or another) is drawn into the production of agricultural products and seeks to supply their own needs for foodstuffs. Obviously, there is no point in talking about the efficiency of agriculture here. The fact that the government proudly calls them “farmers” does not change the essence of things. Whereas a farmer in industrially developed countries has a complex of machines, modern technologies, and a network of infrastructures to service agriculture and to sell its products, our peasant—apart from the proud name of “independent producer”—has only a shovel, rake, and fork at his disposal.

The replacement of commodity production by what is primarily the cultivation of food products for personal consumption appears harmless, but only at first glance. In fact, the negative consequences of this tendency are much more serious for the entire economy. As a result, in the village today it is not uncommon to witness a barter exchange, which has acquired a certain dissemination of late. The low volume of commodity production of peasants inevitably leads to an

absence of money in circulation. The peasants are forced to compensate for this through the direct exchange of products, which one can hardly pronounce a plus in a market economy.

The crisis in agriculture is systemic. Many problems of the village and agricultural branch are a reflection of the general economic situation. And they cannot be resolved within the framework of this branch alone.

The “Dutch Disease” as a Cause of Noncompetitiveness in the Agrarian Sector

It is widely thought that the cause of all the woes of agriculture is the absence of resources for its development. According to this view, investment is wanting because short-term and expensive credits cannot resolve the fundamental problems faced by the agricultural sector of Azerbaijan. That is why, it is argued, agriculture has until now been based on manual labor, and villagers, with their small-scale family operations, can never be expected to produce agricultural products that are competitive in the marketplace.

In fact, the foregoing is merely a consequence. The causes actually lie deeper.

The developmental tendencies in agriculture are such that, in recent years, one can clearly discern the following, extremely unfavorable factor. Namely, on both the domestic market and on the neighboring (and in principle attractive) market of Russia, with increasing frequency we encounter what at first glance seems a paradoxical situation: Azerbaijan’s producers are unable to compete not only with traditional partners (Iran, Turkey, the countries of Central Asia, and so forth), but even with the Russians and other northern countries.

The Azerbaijani peasant, who has raised the traditional vegetables, fruits, and the like, and who comes to the Russian market, is horrified to discover that the products brought from Turkey, which have a more attractive appearance, for some reason are sold much more cheaply.

The domestic market, despite all the barriers of customs, nevertheless finds itself under pressure from cheap agricultural imports. There remains nothing

else for the peasant to do except to cultivate these products for his own personal use. The urban consumer, as before, prefers imports.

Leaving aside the problems that our peasants face when they export goods (various types of levies on the roads and the like), let us try to determine why products raised with virtually the cheapest labor in the world and under the most favorable agro-climatic conditions in the final analysis prove unfit for sale.

The most tangible pressure for peasants, as before, is the monetary-credit and exchange policy introduced by Azerbaijan seven years ago. Once financial stabilization had been achieved in the country, this policy began to work not for the economy, but against it.

As is well known, in 1994 the government—to bring hyperinflation under control—had already undertaken steps to limit the monetary flow into the economy and to shift to a fixed exchange rate for the national currency. By 1996, this policy—which was actively supported by the International Monetary Fund (IMF)—had yielded positive results.

The level of inflation plunged from 1129.1 percent in 1993 to 19.8 percent in 1996. And in the ensuing years, the policy even led to deflation. This now already the second year when the annual level of inflation fluctuates within a range of 1 to 2 percent.

Since 1995, however, the policy of strengthening the manat has gradually complicated the situation for domestic producers, especially peasants. In the space of just four years (1995-1998), the manat rose 12.4 percent against the U.S. dollar. From the position of the real sector, it was not difficult to notice that this exchange rate for the national currency was unrealistic: the manat was growing stronger because of the large volume of hard-currency reserves of the National Bank. And for the presence of the hard-currency reserves, the government had to thank not only the IMF (which did not stint in issuing a large volume of technical credits, especially during the first years of reform, to stabilize the national currency), but also the first receipts from the oil revenues, to be sure, for the present in the form of bonuses from foreign companies to explore contracted areas in Azerbaijan.

The policy of gradually strengthening the exchange rate of the manat inevitably had to aggravate the already difficult position of local producers. However, the unique shock-absorber of the situation that emerged in 1996-1997

was a certain kind of speculation on the investment market of Azerbaijan. The privatization of small and some medium-sized enterprises and the release of privatization checks into circulation (and their subsequent circulation on the secondary market) objectively aroused the interest of foreign investors. The latter counted on servicing the oil companies and investments in the non-oil sectors, such as telecommunications, construction of refineries, and so forth.

For agricultural producers, one cannot unqualifiedly pronounce this a bad period. On the one hand, the relatively high exchange rate of the manat dismantled barriers to the influx of cheap imports into the domestic market. That of course was a source of serious consternation among the producers of agricultural products. On the other hand, a certain upturn on the investment market and the influx of the first large foreign investments gave them an opportunity to sell their goods on a market with relatively greater purchasing power. Even the effect of an austere monetary policy, which gradually reduced demand, did not prevent them from feeling relatively comfortable. To be sure, all these factors worked to satisfy current needs, not to generate long-term investment in the agrarian sector.

A further stimulus came from the sharply increasing volume of incomes earned by Azerbaijani citizens and flowing into the republic from other countries of the Commonwealth of Independent States (CIS). The immense opportunities in Russia and the exchange rate of the ruble were doubly favorable for Azerbaijan. The earnings of Azerbaijanis in Russia, given the exchange rate in dollars, proved considerable, and these were accompanied by the first investments of foreign oil companies. Together, they formed the majority of the income basket in society. By the most modest calculations, the annual volume of income transfers by Azerbaijani citizens from Russia in 1997 amounted to approximately one billion dollars. For comparison, it should be noted that the receipts of the state budget of Azerbaijan in this period were equal to just 643.5 million dollars.

A second favor was the relatively high price of Russian agricultural goods, which prevented them from putting pressure on the Azerbaijani domestic market in the same volume as would later be the case.

After the crisis of 1998 in Russia, the economic situation in Azerbaijan underwent a qualitative change. It is widely thought that the financial crisis of 1998 (and the ensuing sharp devaluation of the ruble) bypassed Azerbaijan. This

was purportedly due to the fact that, since Azerbaijan was not bound to the ruble and did not have active foreign trade relations with Russia (largely as a consequence of the political policies of the Yeltsin government), Azerbaijan could not experience a fall in the exchange rate and other negative consequences, as did happen, for example, in Kazakhstan and Belarus.

In fact, however, the crisis dealt Azerbaijan a blow that was no less intense, but only indirect and much more palpable, for it aggravated the internal economic situation in the country. But if one takes into account the fact that the crisis in Russia coincided with a sharp fall in the price on oil on world markets (it is no secret that the latter provoked the former), one can imagine the full complexity of the situation that beset Azerbaijan.

The nearly fivefold decline in the exchange rate of the ruble was reflected in the economy of Azerbaijan. Russian agricultural products, which (in dollar terms) now proved much cheaper than earlier, “attacked” with incredible force the Azerbaijani domestic market. The government not only did nothing to oppose this pressure, but sometimes (at the level of customs) even abetted it. The statistics eloquently confirm this tendency. Thus, if the volume of imports from Russia in 1997 amounted to 151.5 million dollars, beginning in 1998 it rapidly increased, reaching a total of 193.8 million dollars. In 1999 imports from Russia rose to 225.8 million dollars, and in 2000 reached a record level of 249.3 million dollars. True, the effect of devaluation then abated, and the volume of imports again began to decline. In 2001, for example, imports from Russia amounted to just 153 million dollars (see Figure 1 in the appendix).

This tendency was characteristic not only of Russia. As we shall see, almost the same picture was observed with imports from Turkey after that country suffered a financial crisis in February 2001. If in 2000 the imports from Turkey amounted to 128.5 million dollars, in 2001 they had risen to 148.2 million dollars. Consequently, one can draw the conclusion that such export pressures from large countries (at the foundation of which is the impact of a devaluation of their national currency) have a universal character.

As for Azerbaijan’s exports to Russia, it is obvious that under these new conditions agriculture was thrust into a manifestly untenable position: on the vast scale of the enormous Russian market, the great majority of agricultural products

from Azerbaijan proved unable to compete. As a result, if in the pre-crisis year 1997 the volume of exports from Azerbaijan to Russia amounted to 180.5 million dollars, in 1998 it was only 105.8 million dollars; then, in 1999 it dropped to 83.1 million dollars, and by 2001 had declined to only 77.6 million dollars.

In addition, one should note the repetition of the case with respect to Turkey in 2001: exports to that country had been 105 million dollars in 2000, but after the February crisis sank to a record low of 67.4 million dollars (see Figure 2 in the appendix).

In 2000, the National Bank of Azerbaijan seemingly began to understand that it was necessary to change the policy for setting the exchange rate and officially to proclaim a policy of managed inflation and gradual devaluation of the manat. In reality, however, in lieu of the managed inflation, the result has been the same deflation or only a symbolic (1.6 percent) rise. The exchange rate has decreased by an average of 4 to 5 percent. But this cannot qualitatively change the situation. As before, the domestic producer is caught in the vice of an exchange rate for the manat that is unfavorable for the real sector; monetary limitations then deal the final blow. For comparison, we would point out that the level of monetization (the ratio of the monetary supply to the GDP) in 2001 amounted to 7 percent, whereas that indicator in developed countries is approximately a third of the GDP.

To achieve a fundamental change in the situation, at a minimum it is necessary to do the following.

First, and most important, it is essential to sterilize the excess of hard currency with a simultaneous barrier to funnel it into the coffers of the National Bank of Azerbaijan. That is because the disproportionate hard-currency earnings from the export of oil (the share of which already exceeds 90 percent of all export earnings) objectively impels the National Bank to establish an exchange rate of the national currency at an unrealistic high level. It is necessary to note that, at the end of 1999 (with the creation of the State Oil Fund of Azerbaijan and its accumulation of oil revenues), this question was practically already resolved. It is now necessary to use more correctly these resources, which, at the first stage, should be completely segregated to ensure that they are not diffused (especially through mixing in the budget). In the contrary case, the result can be a kind of intravenous bleeding, and the budget balance can prove ineffective from a macroeconomic

point of view.

Second, the National Bank must renounce an austere monetary policy and choose a policy with a palpable devaluation of the manat. All the requisite conditions for this are now at hand. The creation of an oil fund eased the situation, and the National Bank in the future can more confidently pursue a policy of weakening the manat. However, the 4 to 5 percent annual level of devaluation that the National Bank achieved in the last two years is inadequate, and local producers cannot feel a qualitative change in the situation.

Third, and most important, it is essential to conduct truly fundamental institutional reform and structural transformation. Without this, all the other measures will prove inadequate. This alone is the key to serious successes and to a tangible improvement of conditions for the domestic producer, and it will inexorably lead to a reduced dependency on oil and to the diversification of the economy.

In this sense, the locomotive that can lead the entire branch out of the crisis is the development of the processing sector.

Many of the ills that afflict today's agrarian sector in the country are linked with the virtually inert state of the processing and food complexes in the country. If in the Soviet period these plants were the main consumers of agricultural output, today—because of their inability to function—their place in the economic picture of the country is purely symbolic. Suffice it to say that the food-processing sector accounted for only 13.4 percent of the entire industrial output produced in 2001. As a result, the great majority of goods on the consumer market of the country consist of imports.

Despite the foregoing, the prospects for the development of the agrarian sector in Azerbaijan give grounds for optimism. It must be remembered that Azerbaijan, together with its fertile land and favorable natural climatic conditions, still has a uniquely hardworking people. At the same time, one must also note something else. As the cheapest labor force in post-Soviet space, the Azerbaijani peasant gives exceptional stability to the social order. Thus, in the interests of the entire society, it is time to become seriously engaged with the problems of agriculture and the village.

On the Possibilities and Prospects for the Formation of an Economic System in the Southern Caucasus

Vladimir Papava

The economy of the former USSR was characterized by a high degree of integration of the economies of the constituent union republics and was based on a precise all-union division of labor. This explains why the coexistence of these republics in a single economic space for the long span seventy years made such a deep imprint on their economic systems and shaped their orientation toward a single economy. After the breakup of the USSR, all the newly formed states found themselves facing the same task: the need to create, practically from scratch, independent national economic systems. Each of these economies represented individual components of what had once been a unified complex; they were mutually linked to one another by their structure, the distribution of productive forces, the technologies employed, and the principles of the organization of production.

The situation that emerged after the breakup of the USSR was aggravated by the fact that, in essence, the Soviet economy had already found itself in the grips of crisis.¹ The Soviet economy had revealed the glaring rigidity of its administrative-command structures, which proved incapable of reacting quickly and effectively to innovations. The prolonged mobilization of natural, labor, and capital resources on an extensive basis, together with the rising noneconomic burden and sharp decline in the efficiency of the economy, in the 1980s led to a situation where it became necessary to increase the share of savings merely to keep the system functioning at its current level (that is, without achieving any growth whatsoever). It was during this period that the preconditions for the destabilization and the crisis in the financial system were formed. The crisis process was further

¹For example, see W. Easterly and S. Fisher, "Living on Borrowed Time: Lessons of the Soviet Economy's Collapse," *Transition. The Newsletter about Reforming Economies*, 5:4 (1994).

aggravated by political factors in 1989-1991. As a result, by the time of the breakup of the USSR, the following had already become apparent:

- a decrease in production and investment;
- a disruption of economic relations among enterprises;
- a disintegration of the financial system and the loss of control over the monetary and credit sphere;
- a bankruptcy of foreign policy and treatment of hard currency;
- a degeneration of state-political and economic organizations.

In addition, the diversity of natural climatic conditions, the large amount of natural and human resources, and a number of external factors enabled the Soviet economy to be relatively closed to the world market. The material-technical base of the economy of the USSR, compared with the advanced international standards, in general was obsolescent. After the breakup of a single economic system and the appearance of financial difficulties (both at the level of the newly formed states and at the level of individual enterprises), the country faced a situation where, for all practical purposes, its capacity for technological renewal proved negligible. As a result, the machinery became not only obsolescent but was also worn out. This in turn was the main reason why the majority of goods produced in the post-Soviet countries could not compete on the market (specifically, because of their inferior quality and/or the high costs of production); that of course made it impossible for them to gain entre to world markets and to become actively integrated into the world economic system. This component of post-Soviet economics was essentially dead; its “functioning” had been due to the mechanisms of “necroeconomics.”²

The foregoing pertains, in one way or another, to all the former republics of the USSR and, in particular, to the region of the southern Caucasus.

The relatively small territory of the southern Caucasus (186,100 square kilometers) is distinguished by a great diversity in the landscape and natural geographic conditions. The Caucasus as a whole, but also the southern Caucasus, always was and now to a still greater degree is a conglomerate of contradictions. In recent years, this characteristic has been apparent in the political processes transpiring in the region and in the conflicts between national and ethnic groups.

²V. Papava, “Necroeconomics—a Phenomenon of the Post-Communist Transition Period,” *Problems of Economic Transition*, 44:8 (2001).

The problems in the social-political life of the peoples of the southern Caucasus are of such a large scale in their significance that one must relate them not only to political, social, and moral planes, but also to the economic sphere as well. The initiation of military operations (including in the northern Caucasus and, in particular in Chechnia, which has had an especially negative influence on Georgia) has led to destruction, loss of life, the social problems associated with the presence of a large number of refugees, and the blockade of transportation arteries. All this inevitably had a substantial impact on the economic situation and the realization of production capabilities in the states of the southern Caucasus.

As a result of these political, economic, and other factors, practically all the entities of the southern Caucasus—in one or another degree—found themselves cast into a profound crisis, which enveloped all spheres of their activities and led to a sharp contraction of production, to a high level of inflation, and to a decline in the standard of living. In Georgia, for example, the volume of production of the gross domestic product (GDP) decreased between 1989 and 1994 by 4.5-fold; in Azerbaijan the GDP of 1996 was 42 percent lower than it had been in 1990; the economy of Armenia by 1994 was in severe straits (the GDP of 1993 representing only a third of its level in 1989). Beginning in 1994–1995, thanks to the active implementation of reform,³ one can observe a tendency toward stabilization and economic recovery. However, the consequences of the crisis are so profound that they cannot be overcome in a single year; it is necessary here to carry out a radical, constructive domestic economic policy, to find an optimal combination of interests of all entities of this region, and to make an active effort to attract foreign investment.

The development of the economy in this or that country, to a large degree, depends on how much one takes into account foreign economic factors in the formulation of a country's economic policy. Of particular significance is the need to take into account the main tendencies in international relations and to find a country's own niche in the world economic system. This must become the foundation for determining the strategic lines of economic development and the top priorities of economic reform in the countries of the southern Caucasus.

The economic progress of the states of the southern Caucasus, above all, will be predetermined by the tempo of their integration into the civilized world. If

³V.A. Shul'g, ed., *Ekonomika SNG: 10 let reformirovaniia i integratsionnogo razvitiia* (Moscow: Finstatinform, 2001); I. Maradian, *Geoekonomicheskaia situatsiia v stranakh zakavkazskogo regiona i ekonomicheskaia struktura etikh gosudarstv*, *Tsentral'naia Aziia i Kavkaz*, 2000, no. 1.

one considers the current condition of the economy and productive potential of the states of the southern Caucasus, the goal of integration cannot be thought to be among those that are easily resolved. To be sure, it is impossible to say that the region of the southern Caucasus, despite the political complications that do exist, is not at all isolated from the rest of the world. First, this region is a component of the Commonwealth of Independent States (CIS).⁴ Second, Azerbaijan, Armenia, and Georgia are members of the Black Sea Economic Alliance. Third, all three states of the southern Caucasus almost simultaneously signed agreements with the European Union for cooperation and partnership; this laid the basis for bilateral commercial and economic relations with many countries of the world community. However, one cannot see all these aspects of international integration as sufficient to bring about the region's inclusion into the world market.

In the opinion of critical experts, today the CIS is experiencing a certain stagnation with respect to its integration processes. Moreover, for a number of well-known reasons, it is in no position to ensure the introduction of international standards of production; on the contrary, it promotes the formation of limits to the integration processes within the framework of the CIS (in a manner analogous to the closed system of productive cooperation that had characterized the economic system of the USSR).⁵

The Black Sea Economic Alliance, although possessing great prospects and therefore demanding special attention, nevertheless is still a relatively new inter-state regional organization. For the present, it does not have the requisite level of integration and active interrelations to exert a substantial influence on the economic development of its member-states.

Cooperation with the European Union and economically developed European states, at the present time, cannot be realized on the basis of an equal partnership. Rather, here is a process of providing aid in mastering and implementing democratic principles in ordering social and political life and in introducing market mechanisms into the economy.⁶

Moreover, the advanced countries of the world for the present are taking a wait-and-see position as they follow the course of events in the southern Caucasus.

⁴For example, see D. Matsnev, "Strany Tsentral'noi Azii i Kavkaza v SNG: ekonomicheskii aspekt," *Tsentral'naia Aziia i Kavkaz*, 2000, no. 1; L.P. Kozik and P.A. Kokhno, *SNG: realii i perspektivy* (Moscow: Izdatel'skii dom "Iuridicheskii mir VK).

⁵M.B. Olcott, A. Åslund, and S.W. Garnett, *Getting It Wrong: Regional Cooperation and the Commonwealth of Independent States* (Washington, D.C.: Carnegie Endowment for International Peace, 1999).

The view is widespread that the southern Caucasus is, unfortunately, a “hot spot” that lacks sufficient political and economic stability to attract economic partners.

At the same time, one must also take into account the fact that the relatively small size of the countries of the southern Caucasus (with a total population that does not exceed 17 million), all things being equal, determines the correspondingly small scale of their markets. If one looks beyond the existing conflicts in the region and examines the theoretical possibility of forming a single market in the southern Caucasus, then even in this idealized case the scale of this market is nonetheless still small and cannot provide a major attraction for substantial investments. This idealized market can be “covered” by the investments being made either in Russia or in Turkey.

All this demonstrates the need to find opportunities for mutual assistance among economic entities in the states of the southern Caucasus with respect to laying the preconditions for rapid, stable development. It also shows the need to find opportunities to establish a system of strategic economic partnership (and not simply cooperation) in the southern Caucasus.⁷ Only joint (even if, initially, informal) efforts will facilitate the effort to find common spheres for attracting foreign investment to the region.

As for the question of attracting large-scale investments to the southern Caucasus, the main task here is the need to reduce the high risk of long-term investments. It is this factor that has made investment in the southern Caucasus so unattractive. At the same time, the region has spheres that could become objects of special interest for foreigner investors. In this respect, it is sufficient to cite the oil of the Caspian basin⁸ and the Eurasian transportation-communications corridor,⁹ linking Europe and Asia through the region of Central Asia and the southern Caucasus.¹⁰ All this allows one to conclude that the southern Caucasus is acquiring a special function and that many states and leading companies of the world have

⁶For example, see A.M. Gegeshidze, “The South Caucasus: Getting Close to Europe?” *Marco Polo Magazine*, 1999, no. 1.

⁷V. Papava and N. Gogatadze, “Prospects for Foreign Investments and Strategic Economic Partnership in the Caucasus,” *Problems of Economic Transition*, 41:5 (1998); V. Papava and N. Kakabadze, “Strategicheskoe ekonomicheskoe partnerstvo na Kavkaze,” *Zovnishnia torgivlia*, 2000, no. 2.

⁸F. Asadov, “Neftianye karavany XXI veka na Velikom shelkovom puti: perspektivy Azerbaidzhana i Kazakhstana,” *Tsentrāl'naia Aziia i Kavkaz*, 2000, no. 6.

⁹A. Gegeshidze, “Eshche raz o Velikom shelkovom puti,” *Tsentrāl'naia Aziia i Kavkaz*, 1999, no. 3(4): 172.

¹⁰A. Martirosian, “Velikii shelkovyi put': etapy vosstanovleniia,” *Tsentrāl'naia Aziia i Kavkaz*, 2000, no. 6.

made it a strategic goal to consolidate their presence in this region.

The increase in the rate of economic growth in Azerbaijan can be mainly attributed to the growth in the volume of oil production and to the development of the petroleum refining branch.

At the same time, both the problem of developing the oil branch and the future economic development of the entire southern Caucasus, to a large degree, depends on creating the transportation arteries of TRACECA (Transport-Corridor-Europe-Caucasus-Central Asia).

TRACECA¹¹ today is viewed as a transit corridor, which will supplement and develop all the existing routes, in the first instance, the European routes. In this regard, it represents an opportunity to link the transportation systems of the Black, Caspian, Adriatic, and Mediterranean Seas.

No less important is the task of resolving the question of transporting energy resources through a pipeline system. In particular, the Azerbaijani-Georgian route for shipping oil has become one of the top-priority, large-scale projects in Georgia and has attracted considerable foreign investments. At the same time, the realization of this project creates the preconditions for more active investment in other spheres of the Azerbaijani and Georgian economies.

At the same time, this project would not have a future were there not also a parallel project to ship oil from Azerbaijan through Russia. That is because, given the conditions of potential conflict and the fact that the oil pipelines cross through or near to "hot spots," the existence of alternative pipelines is critical. Consequently, this example shows that not only Azerbaijan and Georgia, but in the question of shipping early oil both Georgia and Russia can indirectly be seen as strategic economic partners, even if, unfortunately, Russia for all practical purposes has never acknowledged as much.¹²

It is particularly important for the economies of Georgia and Armenia that the project for a transportation corridor through Georgia, Armenia, and Iran be realized. Such a corridor is of fundamental significance for the development of a strategic partnership between Georgia and Armenia.

In examining the various aspects of economic development of an entire

¹¹A. Rondeli, "TRACECA: A Tool for Regional Cooperation in the Caucasus," *Marco Polo Magazine*, 1999, no. 1.

¹²R.M. Avakov and A.G. Lisov, eds., *Rossia i Zakavkaz'ea: realii nezavisimosti i novoe partnerstvo* (Moscow: ZAO "Finstatinform," 2000).

geographic region and the mutual relations of the states located here, it is also necessary to touch upon the question of economic competition between the individual countries in this region.

According to the theory of market competition, various levels of competition are foreseen: at the firm level, at the branch level, at the country level, and at the regional level. As a rule, the competitors should be characterized by a more or less identical economic power and identical definition of their economic interests, which in turn determine the conjunction of their economic claims. The competitiveness of a country depends, in the first instance, on how productively it makes use of its natural, labor, material, and financial resources. At the same time, any competition is, to a certain degree, a stimulus for improvement. If there were no international competition, the level of productivity in each individual country would be virtually independent of the situation in other countries. But the international flow of goods and capital represents an opportunity to increase the productivity in exploiting a country's resources, eliminates the need to produce all goods and services on its own, and enables a country to specialize in those branches of the economy and market segments where it is relatively more competitive.

Given the foregoing, one can draw the practical conclusion that, in economic terms, for example, Azerbaijan and Georgia are not strategic competitors. This is due to the fact that Azerbaijan has oil and gas, while Georgia has sea access to the ocean and direct borders on Turkey. Moreover, both countries are located on the TRACECA route; each has its own productive potentials, which in a number of cases are unique. All this means that Azerbaijan and Georgia cannot be seen as competitors, but rather are strategic economic partners.

Georgia has a vested interest in seeing that Caspian oil and natural gas (and not only these items) are transported to the West across its own territory. That is, simultaneously, in the interests of Azerbaijan, for in this case all possible cargoes from East to West—and vice-versa—will pass through its territory.

At the same time, the lack of economic competition between Georgia and Azerbaijan in no way should be seen as causing a lack of stimuli for development. After all, these countries have other country-competitors. But they themselves should be seen as economic partners in inter-regional competition. The economic partnership of Georgia and Azerbaijan can become a magnet (as, to a certain

degree, is already confirmed in practice) for attracting other entities not only to the southern Caucasus, but throughout the entire Caucasus. Unfortunately, however, not all are willing to recognize publicly the advantages of a strategic economic partnership for the region.

In turn, a strategic economic partnership is the foundation upon which one can, and should, construct an economic system for the southern Caucasus.

The Administrative Elite of Uzbekistan: After 11 September 2001

Evgenii Abdullaev

The events that followed the terrorist attack on the United States on 11 September 2001 have caused political scientists and observers to give more attention to the post-Soviet states of Central Asia. A region that previously had been on the periphery of “great politics” suddenly, within a couple of months, became a mainstay of the front pages of the main newspapers; the states located in this area gradually ceased to figure under the amorphous and derisive rubric of “stan” countries.

The leading focus of such interest is Uzbekistan, which is called the most important ally of the United States in this region and which proved more adept than the other Central Asian states in making its air bases available for the antiterrorist operations in Afghanistan. Uzbekistan’s appeal to combat terrorism and religious extremism, which it has been pressing ever since the mid-1990s, was not only heard but appreciated under these new circumstances. Thus, Secretary of Defense Donald Rumsfeld made the following statement during his visit to Tashkent on 5 October 2001: “The interest of the U.S. in Uzbekistan, it should be well understood, precedes the events of September 11. . . . And the interest of the U.S. is of a long-standing relationship with this country and not something that focuses on immediate problems alone.”¹

At the same time, this growing interest has been accompanied by a widening audience for the traditional critics of the authoritarian regimes in Central Asia—viz., the activists of human rights organizations, the representatives of various liberal foundations, “independent researchers,” and so forth.² Moreover,

¹Cited in Z. Echanova, “Uzbekistan: Rumsfeld Visit Builds Hopes of Closer Relations with U.S.” (<http://www.rferl.org/nca/features/2001/10/08102001110340.asp>).

²As was pointed in the very opening of the recent report by Human Rights Watch in Uzbekistan, “the new U.S.-led campaign against terrorism dramatically changed Uzbekistan’s international position, but its appalling human rights record remained unchanged.” See Human Rights Watch, *World Report 2002. Europe and Central Asia: Uzbekistan* (www.hrw.org/wr2k2/europe22.html) See also “Ex-Soviet Uzbekistan Emerges as Key State in U.S. anti-terror Campaign” (www.cdi.org/russia/174.cfm##5).

endorsement of this criticism has also come from many foes of the current foreign policy of the White House—that is, people in the United States itself as well as observers in other countries who are ill-disposed toward the United States. For all these people, criticism of Uzbekistan provides a convenient pretext to criticize the administration of George W. Bush and, more generally, the notorious “double standards” of American policy. By characterizing the political system in Uzbekistan as authoritarian or even “dictatorial,” the critics seek to draw a parallel between Uzbekistan and the illiberal regimes that the United States has supported at various stages in the past (for example, Chile, Pakistan, China, and so forth).

As a result, one finds a juxtaposition of two different types of representations of Uzbekistan: the *apologetic* (which gives an unequivocally positive assessment of the foreign policy of Uzbekistan—viz., as the most reliable regional partner of the United States in its operations in Afghanistan), and the *hypercritical* (which offers an exaggerated portrait of Uzbekistan and seeks to demonstrate the “incoherence” of official Washington in its choice of partners).

Interestingly, this situation—which involves a clash of paradigms substantially replicates the picture of Russian-Uzbek relations in the mass media in 1999-2000 (i.e., amidst the change in Russian leadership and the plan to reconsider Russian policy in Central Asia). During this period, the majority of Russian mass media gave an extremely positive assessment of Uzbekistan as the “main regional partner of Moscow” and as a “shield against the penetration of terrorism and religious extremism in Russia.” At the same time, the Russian mass media hostile to V. V. Putin (along with Western observers and politicians) intensified their criticism of the Uzbek regime as extremely authoritarian; they also envisioned the rapprochement between Russia and Uzbekistan as tending to reinforce authoritarianism in Russia itself.

Consequently, the present duality in assessments of Uzbekistan, to a great degree, derives not so much from the situation in the country or from the alignment of foreign powers (i.e., the main “players” seeking to have an influence in Central Asia), as it does from the alignment of political forces *within* these “player-countries.” Naturally, both the criticism and apologetics provide a somewhat one-sided and tendentious picture of the situation in Uzbekistan. Given such an approach, authoritarianism and a Western orientation prove to be isolated

from one another; at the same time, this also gives rise to a superficial picture about the causes and mechanisms of the ruling elite in Uzbekistan. This essay seeks to analyze the genesis and transformation of the governing elites of Uzbekistan and to take into account the specific features of their decolonization and Westernization.

Of the three methodological approaches to the problem of governance (managerial, political, and legal), for the purposes of this essay the author has adopted a political approach. The analysis will concentrate on the reflection of group political, economic, and social interests in the administrative elites of Uzbekistan, taking into account, however, the social-political context in which these elites find themselves. As one of the adepts of the political approach (H. Seidman) has correctly noted, “the executive branch structure is in fact a microcosm of our society. Inevitably it reflects the values, conflicts, and competing forces to be found in a pluralistic society.”³ Although by no means can all societies (including Uzbekistan itself) be called pluralistic, Seidman’s comment seems relevant to an analysis of the Uzbek administrative elites.

For purposes of this study, we shall use the term “administrative apparatus” as the more value-neutral equivalent to the Weberian “bureaucracy.”⁴ The term “administrative elites” of Uzbekistan denotes the administrators in the middle and upper ranks; they are not directly associated with making political decisions, but actively influence both the preparation and realization of such a policy. This is the most firmly ensconced, stable elite group in Uzbekistan, and its parameters differ from those of the less stable elites—i.e., the political, economic, intellectual, and other categories of elites.

The *political elite* in Uzbekistan (for lack of a clearly organized political opposition, and the depoliticized nature of legislative and judicial power, etc.) at the present time represents in effect an extension of the administrative elites. Namely, they are recruited primarily from the ranks of the latter, a process that is quite ordinary for states with strong presidential power.

The *economic elite* is also quite firmly interwoven with the administrative elites—both indirectly (through family and local connections) and directly (with

³H. Seidman, *Politics, Position, and Power* (New York: Oxford University Press, 1970), 13.

⁴In the judgment of John A. Armstrong, the distinction between ‘administration’ and ‘bureaucracy’ . . . has been a matter of disciplinary bias. Political scientists prefer to use administration to designate formally non-political activities of the governments, while sociologists since Max Weber have preferred bureaucracy.” See his book, *The European Administrative Elite* (Princeton: Princeton University Press, 1972), 6.

many administrators informally combining work in state administration with commercial activities).

As for the *intellectual elites* (scientific, cultural, mass media, and so forth), in a situation characterized by a reduction in state subsidies and an insignificant level of commercialization, this elite has fully maintained its former dependency on the administrative elite. Other elites (military, religious, etc.) are also dependent and, to a greater or lesser degree have been incorporated into the administrative apparatus and placed under its control.

Thus, the administrative elite represents the most important social category in contemporary Uzbekistan, for it has assumed, in addition to its immediate functions, some of the tasks and roles of other elites (political, economic and so forth). Such a concentration of functions has its roots both in the remote and in the recent history of Uzbekistan—that is, the critical moments of the second half of the 1980s and early 1990s that the administrative elite has had to experience. Therefore it is important to consider, if only briefly, the historical stages in the formation of the profile of the contemporary administrative elite of Uzbekistan.

Genesis of the Contemporary Administrative Elite of Uzbekistan

A developed and diversified administrative system existed among the sedentary peoples on the territory of Uzbekistan from ancient times. Right up until the end of the nineteenth century, this system quite steadily reproduced itself, successfully resisted both the expansion of nomadic tribes with a simpler administrative structure,⁵ and the attempts of local religious and secular charismatic leaders to take away part of the power and privilege of the administrative apparatus. The durability of this apparatus was ensured by the stability of income from the agrarian communities and the caravan trade, but also by the rather high level of education of officials who were recruited from the ranks of religious, scientific, and literary elites. The participation of religious elites in the administrative system gave

⁵As N. N. Kradin has aptly observed, “the nomadic aristocracy . . . , as a rule, was excluded from the governance of conquered territories. In addition, an intervention in administration was often simply impossible, given the complexity of the bureaucratic apparatus of the sedentary, agricultural states.” See N. N. Kradin, “Kochevye imperii: genezis, rastsvet, upadok,” *Vostok*, 2001, no. 5:25.

it additional ideological legitimacy; however, the main symbolic source of legitimacy in the administrative apparatus, as in all monarchical systems of the world, was the sacred aura of the ruler-monarch. In other words, Karl Wittfogel's thesis can be applied to the Central Asian states: in traditional Eastern societies all power belonged to the administrative elites.⁶

Russian colonization⁷ of Central Asia laid the foundations for a period of turbulent transformation of the administrative system of Uzbekistan, a process that lasted for an entire century. The main agent of this transformation was the Russian state, which carried out an administrative restructuring of Uzbekistan, a Westernization of elites (in its Russian variant), and the creation of a "parallel elite"—producers and technocrats, who, as a rule, were recruited from a non-indigenous, European population.

In periods when Russian control was somewhat weakened, the traditional administrative system of Uzbekistan demonstrated a natural attempt to regenerate and to reclaim the lost power and privilege. However, these periods did not continue for long; each time the reinforced administrative elite was subjected to repression and various kinds of restructuring. Thus, in the beginning of the 1920s, the former aristocratic elite was totally destroyed; at the end of the 1930s, the top ranks of the new Soviet *nomenklatura* were decimated by repression; finally, in the mid-1980s (in the midst of the infamous "cotton case"), hundreds of administrators were arrested, with a 90 percent turnover in personnel in the composition of the upper administrative echelon.

Moreover, the traditional pillars upon which the legitimacy of the administrative apparatus had been based also proved to be demolished: the local (Central Asian) Islamic tradition and the sacred figure of the ruler. The repression of Islam (coinciding, as a rule, chronologically with the repression of the Uzbek administrative elites) put an end to its influence on the process of generation and

⁶See K. Wittfogel, *Oriental Despotism: A Comparative Study on Total Power* (New Haven: Yale University Press, 1957).

⁷Following J. Osterhammel, the author understands "colonization" to designate a "relationship of domination between an endogenous . . . majority and minority of foreign invaders, in which the fundamental decisions affecting the lives of the colonized people are often defined in a distant metropolis." See Osterhammel, *Colonialism: A Theoretical Overview* (Princeton: Markus Wiener Publishers, 1997), 16-17. Regarding the applicability of the term "colonialism" to the period of history of Uzbeks within the Russian Empire and Soviet Union, see C. Cavanaugh, "Central Asia's Colonial Past and Why It Matters," *Central Asia Monitor*, no. 5/6 (2001): 9-17 (also the source of the citation from Osterhammel).

legitimizing elites. At the same time, the Marxist-Leninist ideology could not perform an analogous legitimizing role. Whereas Islam possessed, from ancient times, an independent authoritative theological tradition within the territory of Uzbekistan, the right to interpret Marxism was also reserved to the ideological apparatus in Moscow.

As for the sacred aura of the ruler, this had generally been ascribed to those leaders of the republic who had the greatest power and authority, but who were then subjected to ostracism (either during their lifetime or posthumously). Such was the fate of A. Ikramov and F. Khodzhaev, who were purged as “enemies of the people” in 1937, and a half-century later, Sh. Rashidov (whose name was besmirched with insinuations about the cotton case); only U. Iusupov, the republic leader in the 1940s, was a partial exception to this rule. Revealingly, attempts to memorialize well-known Central Asian rulers of the past (for example, Temir or Tamerlane, Shaybaniy Khan, or Bobur) were not encouraged. However, in the case of the last named, a certain exception was made (as a brilliant poet);⁸ an analogous exception was also made for another ruler in ancient times, Ulugbek, a scholar astronomer. But these exceptions served only to confirm the rule.

Finally, during a century of development within the framework of Russia, especially its Soviet phase, the Uzbek ruling elite took shape precisely as an *administrative*, not *political*, elite: all of the most important political decisions pertaining to Uzbekistan were taken in Moscow, at sessions of the Politburo of the Communist Party, where the Uzbek leadership had virtually no influence. During the entire period only two Uzbeks were members of the Politburo; it suffices to compare that figure with the seventeen Ukrainians, six Belorussians, and six Georgians who belonged to the central political organ.⁹ This is all the more striking given the fact that Uzbekistan was the third largest republic in the Soviet Union. However, even those political decisions that were taken within Uzbekistan itself had of course first had to be prepared in collaboration with the administrators sent

⁸As a result of discussions at the government level in the 1970s, Shah Bobur was “rehabilitated”; his bust was placed, along with those of other Russian and Uzbek writers, in the center of Tashkent. However, although Bobur was rehabilitated as a “writer,” there was absolutely not a word of praise about him as a ruler—at the very time when Russian historiography (ever since the late 1930s) had in effect canonized many Russian princes and tsars (for example, Alexander Nevskii, Ivan the Terrible, Peter the Great, and so forth).

⁹See V. A. Tishkov, *Ocherki teorii i politiki etnichnosti v Rossii* (Moscow: Institut etnologii i antropologii Rossiiskoi akademii nauk, 1997), 226.

from Russia; such decisions were never taken without the approval of the Russian administrators. This became especially evident in the mid-1980s, when—at the height of the cotton case—dozens of administrators were dispatched from Russia to replace the “bribe-takers” who had been removed from their position.¹⁰ The military elite was also non-indigenous and consisted mainly of ethnic Russians.

Thus, at the time that Uzbekistan achieved its independence as a sovereign state, it lacked a real political elite. Indeed, its administrative elite had disintegrated and become demoralized by the “cotton case,” by the renewed pressure on Islam (many administrators being subjected to penalties for observing religious rites), and the subsequent toppling of the authority of the ruling figure, Sharaf Rashidov. Moreover, in the late 1980s, against a background of an economic situation that was already deteriorating, Moscow significantly reduced its subsidy for Uzbekistan and froze several large projects that aimed to address the most acute problems then facing the republic. This was, first and foremost, the project to save the Aral Sea by diverting some of the river water from southern Siberia, as well as the project to rechannel surplus labor resources from Uzbekistan to Russia. Both projects were initiated but, under various pretexts, terminated; as a result, surplus water resources, which cause significant damage through annual flooding, remained in Russia;¹¹ the redundant labor forces, similarly, also stayed put in Uzbekistan.

At the same time, so far as the administrative elites were concerned, the century of colonization not only had destructive consequences but also served to consolidate them as a group.

First and foremost, this period brought about a significant modernization of the elites and used them as instruments of power. They came to dispose of almost all the modern instruments of control and coercion—a powerful law enforcement system (which helped to realize total control over the population) and the means of mass information (which make it possible to indoctrinate the

¹⁰One should name, above all, the second secretary of the Central Committee of the Communist Party of Uzbekistan, Anishchev; the deputy chairman of the cabinet of ministers, Ogarek; the deputy chairman of the Presidium of the Supreme Soviet of the Uzbek Republic, Romanovskii.

¹¹As a political scientist in the Russian Federation, S. G. Kara-Murza, points out, “rejection of this program [to divert the rivers], at first glance, did not affect directly the vital interests of the majority of the population of the central part of the USSR, which made it simpler to manipulate their views. Dissatisfaction of the ‘Asians’ only added zest to the spectacle and played into the hands of the perestroika types.” See S. G. Kara-Murza, “Chernyi mif o ‘bol’shikh programmakh’ v SSSR: ot kampanii protiv ‘povorota rek’ k raschleneniiu ‘imperii’” (www.e-journ.ru/p_time-st1-9.html).

population).

Second, the Soviet era preserved and even intensified the principle of noneconomic coercion—which, in fact, had been the foundation of the administrative apparatus of the sedentary agricultural peoples of Central Asia in the course of many centuries. Moreover, collectivization and the unprecedented intensification of the agrarian sector in Uzbekistan significantly expanded the traditional basis of governance and exploitation—that is, with respect to the rural communal population. The cultivation of cotton—an agricultural crop that demands the use of a large volume of low-qualified manual labor—preserved and replicated the semi-servile character of this exploitation. It was no accident that precisely the cultivation of cotton contributed to the maintenance of slavery in the American South until the middle of the nineteenth century; indeed, until today the main producers of cotton (with the exception of the United States) are countries with an administrative system of the authoritarian type.

Third, the Soviet period witnessed a significant renewal of the elites of Uzbekistan—that is, an influx of “fresh blood.” The mechanism for replenishing this elite became more flexible and more democratic. The path to an upward career proved open for those coming from the lower social orders; many of these people occupied leading positions on the basis of their achievements, talent, and energy. Although there were surely many obstacles to this upward mobility (party membership, loyalty, mastery of the Russian language, and so forth), in the Soviet period such criteria did not pose a serious impediment to a career for those from the lower ranks of society. In addition, all this led to a diversification in the ethnic composition of the administrative elites: the Iranian-speaking substratum of the bureaucracy received substantial new complements from the Turkic-speaking and Slavonic-speaking groups (Russians and Ukrainians).

Nevertheless, confirmation of the change in the social and ethnic basis for the formation of elites in the Soviet period must also include significant qualifications. Thus, people from the former elite still continued to hold important positions, both administrative and religious; that is particularly true of those from the “blue-blooded” groups (the Seiids, Hodzhi, and others).¹² Although

¹²S. Abashin has noted the following: “Although the social status of the ‘blue-blooded’ has declined, its representatives have managed to preserve their privileged position in society. . . . A society that had embarked on the path of enormous changes needed many social and psychological qualities that, in the course of centuries, had been formed among the blue-blooded.” See S. Abashin, “‘Ok-suiak’–musul’manskaia elita Tsentral’noi Azii,” *Tsentral’naia Aziia i Kavkaz; obshchestvenno-politicheskii zhurnal*, 2000, no. 6(12):78.

the service record of many top administrators at the end of the 1980s showed that they had begun their careers as factory workers, a large part of these “proletarians” actually came from families in the *nomenklatura* elite, for they had gone off to become temporary workers in a factory in order to facilitate their career and to avoid criticism of “family connections.”

In addition, in the course of the entire Soviet period, the position of the “Iranian” substratum remained quite resilient: the Iranian-speaking people from Samarkand and Bukhara, the traditional centers of administrative power, as a rule, were better suited for office work and found it easier to make a career. Finally, despite the significant proportion of Russian administrators in the administrative elites, they were very poorly integrated into the local elites, did not seek to intermarry with them, and did not have the mechanism of family and local ties at their disposal. In addition, they were quite thinly represented in the administration of agriculture, the main branch of the Uzbek economy.

Thus, although the administrative elite of Uzbekistan was deprived of its traditional legitimizing basis (local Islamic tradition and the sacred figure of the ruler) during the Soviet period, it retained control over the agrarian sector and, in part, over trade—that is, the traditional sources of their incomes. But they also gained control over a powerful repressive apparatus and system of ideological indoctrination. Notwithstanding Moscow’s efforts to change both the social and ethnic base for the formation of the elites of Uzbekistan, the traditional hierarchy each time demonstrated an amazing capacity to regenerate itself, to expel the obvious “aliens,” and to sabotage undesired changes. All this was significantly intensified amidst the uncertain social situation at the end of the 1980s.

The Transformation of Administrative Elites in the 1990s: Problems of De-Russification and Westernization

In the 1990s, Uzbekistan carried out a general decolonization—a phase common to all the former colonial states once they gained their independence. This period brought accelerated state-building: the growth of the administrative apparatus, the introduction of new symbols, a redistribution of power within the

ruling elite, and a renewal of that elite through the infusion of a new generation of administrators. Finally, there has been—naturally, on a new level—a return of the administrative system to that model of governance and practices that had existed in the precolonial period. In other words, despite the fact that, after the acquisition of independence, the institutions of authority and administration have been formally preserved or even modernized, there has been a partial restoration of traditional, precolonial and premodern relations.

The rate at which decolonization is realized can be accelerated or slowed, while its character can be either peaceful or conflictive. Among the post-Soviet countries, Lithuania or Estonia can serve as an example of the most accelerated and peaceful decolonization; Tajikistan, by contrast, underwent a rapid but conflictive decolonization, the result of which was a partial Russian re-colonization of the country.¹³ It should be pointed out that many of the signs of decolonization described above were also to be seen in Russia itself; moreover, for Russia, this process proved quite conflictive and protracted; in our judgment, it did not reach its culminating point until the end of the 1990s.

With respect to Uzbekistan, the process of decolonization in this state can be described as rather non-conflictive and protracted. Strictly speaking, those conservative measures that ensured the absence of an open conflict of interests also caused the slowed, or gradual, path of decolonization. By avoiding radical reformist steps and by combining partial reforms with a restoration of a traditional, precolonial strategy of administration, the elites provided a quite non-conflictive transfer of power from the party-industrial elites to the economic and law-enforcement elites, from the ethnically diverse elites (with a predominance of Russians) to indigenous elites. There was also a reestablishment of the traditional status quo of administrative elites in Uzbekistan (coupled, simultaneously, with their undergoing a certain transformation). The author agrees with C. Dollerup in distinguishing two fundamental, closely intertwined factors at work in the social-psychological transition in Uzbekistan: de-Russification and Westernization.¹⁴ In

¹³This supports the hypothesis of A. Etkind and S. Lur'e about the special character of Russian colonization in Central Asia and the Transcaucasus—viz., as the result of attempts by Russian elites to “colonize” their own (Russian) people. See A. Etkind, “Fuko i tezis vnutrennei kolonizatsii: postkolonial'nyi vzgliad na sovetское proshloe,” *Novoe literaturnoe obozrenie*, 2001, no. 49; S. Lur'e, “Evraziia: problemy sosedstva kul'tur i mezhkul'turnogo vzaimodeistviia” (www.traditio.ru:8101/lurie/eurasia.htm).

my view, these quite fully reflect the processes of decolonization of the Uzbek elites. Both these processes (externally independent of each other, but rather closely related) were completed by the end of the year 2001, having lasted a decade.

1. De-Russification of the Elites: Personnel, Language, and Orientation

The de-Russification of the administrative elites of Uzbekistan represents a complex, multifaceted process. One can distinguish three main elements here:

- A. the withdrawal of non-indigenous administrators from their positions, which is associated with decision-making and access to resources;¹⁵
- B. the exclusion of Russian language from its dominant position in administrative paperwork;
- C. a shift from the pro-Russian orientation of elites (politically, culturally, economically, and so forth) in favor of an orientation toward the countries of the West.

Let us examine each of these elements in the de-Russification more closely.

A. Change in the Composition of Personnel

The exclusion of non-indigenous (mainly Russian) administrators from the upper echelon of administrative power proceeded in a manner that was relatively free from conflict. First, many of them hastened to transfer themselves to leading positions in Russia itself. That was all the more possible because Russia itself, in the first half of the 1990s, underwent a significant growth in its own state apparatus, creating a sufficient number of “landing spots” for emigre VIPs. Second, the crisis that beset industry in Uzbekistan (because of the disruption of its former ties) sharply reduced the weight of the Russian-speaking elite, who were

¹⁴C. Dollerup, “Language and Culture in Transition in Uzbekistan,” in: *Post-Soviet Central Asia*, ed. T. Atabaki and J. O’Kane (London, New York: Tauris Academic Studies, 1998), 144.

¹⁵On this process, see M. B. Olcott [M. B. Olcott], “Emerging Political Elites,” in: *The New Geopolitics of Central Asia and Its Borderlands*, ed. A. Banauazizi and M. Weiner (Bloomington, Indianapolis: Indiana University Press, 1994), 46, 54.

primarily an industrial elite. On the contrary, the emphasis on the development of agriculture and the attempt to achieve agricultural self-sufficiency intensified the position of local indigenous elites, who had traditionally dominated this sector of the economy. Finally, as has been pointed out, Russian administrators in Soviet Uzbekistan were very weakly integrated into the indigenous system of kinship and local ties;¹⁶ instead, they were more oriented toward Russian administrative, industrial, and scientific centers, and they often preferred direct funding from these centers to participation in the redistribution of resources at the local level.

However, if the local elites shared a consensus with respect to the need for a “velvet” removal of Russian administrators from key positions, the situation was much more complicated with regard to the massive exodus of Russian administrators at the middle and lower ranks. On the one hand, their departure reduced many of the tensions between nationalities in the administrative system that had become rather acute by the beginning of the 1990s. In addition, this freed up additional service positions and associated privileges (albeit not as significant as those made available from the upper echelon). On the other hand, as a result of the fact that Uzbekistan gained sovereignty, there commenced a process of structural growth of the administrative apparatus, with the emergence of new ministries and agencies and the fragmentation of old ones. The result was a sharp increase in the demand for administrative personnel. Given the fact that a significant part of the qualified Uzbek administrators in the early 1990s shifted to the sphere of entrepreneurship, the country experienced a rather acute “cadres famine” in the administrative system. In this respect, the Russians faced the prospect of playing, for a certain period, the role of a “mobilized diaspora” (J. Armstrong’s term),¹⁷ and their departure was therefore exceedingly undesirable. Moreover, in the course of the first half of the 1990s, there were serious fears that the oppression of Russians—blatant or imagined—could be used by Moscow to justify intervention in the internal affairs of Uzbekistan.

Therefore, in 1992-1993, the central press of Uzbekistan periodically published materials indirectly expressing concern about the growing migration of Russians. Particularly intense was the resonance to an article entitled “Russians

¹⁶See J. Chinn, *Russians as the New Minority: Ethnicity and Nationalism in the Soviet Successor States* (Oxford: Clarendon Press, 1996), 221.

¹⁷J. A. Armstrong, “The Ethnic Scene in the Soviet Union: The View of Dictatorship,” in: *Ethnic Minorities in the Soviet Union*, ed. E. Goldhagen (New York, Washington: Frederick Praeger Publishers, 1968), 7.

against the Background of the Mosques,” which had appeared in one of the leading newspapers of the Russian Federation in February 1992.¹⁸ That article had given an exceedingly pessimistic assessment of the status of Russians living in Uzbekistan; it predicted that almost half would leave Uzbekistan because of oppression on the part of the local population, but also because of the “Islamic threat.” On two occasions the press service of the President of Uzbekistan issued statements seeking to refute this article.¹⁹ Negative comments about the article also came from representatives of the indigenous elites (a deputy of parliament, a high-ranking party functionary, and so forth).²⁰ It was within this context that the mayor of Tashkent, A. Fazylbekov, gave an interview that was published and became rather well-known; he expressed particular concern about the migration of the Russian-speaking population from Tashkent and promised to make every effort to ensure good relations among the nationalities.²¹ After 1993, the subject of the migration of the Russian population was no longer openly discussed—either in the press or at the official level. A massive exodus of Russians from Uzbekistan did not ensue; nor did Moscow play the “Russian card.” A significant part of the Russians continued to work in the middle range of the administrative system of Uzbekistan, without experiencing any kind of serious infringements of their rights. Characteristically, of the Russians polled in Tashkent in 1994 about their experience since the declaration of independence, only one-third reported a violation of their rights to promotion in service.²² That is a rather good indicator if one takes into account the general social and psychological discomfort that the non-indigenous peoples of Uzbekistan found themselves in 1991-1994.

Nevertheless, as a result of the migration, the “natural habitat” of representation of Russians in administration significantly contracted, as it came to be limited to Tashkent and a few small industrial cities (Chirchika, Novoi, and so forth). In addition, by 1997 the government completed its institutional amalgamation of the administrative apparatus; as a consequence, the need for Russians as a “mobilized diaspora” decreased accordingly. A significant influence on this process resulted from the decline in economic activity in Uzbekistan that began in 1997, which was accompanied by a bolstering of administrative control

¹⁸D. Sabov and I. Cherniak, “Russkie na fone mecheti,” *Komsomol'skaia pravda*, 4 February 1992.

¹⁹*Pravda Vostoka*, 18 February 1992 and 20 February 1992.

²⁰*Pravda Vostoka*, 8 February 1992 and 11 February 1992.

²¹*Pravda Vostoka*, 7 February 1992.

²²N. M. Lebedev, *Noviaia russkaia diaspora* (Moscow, 1995), 92.

over private entrepreneurship. As a result, that triggered a significant egress of Uzbeks from the business sphere into the administrative system—above all, into organs associated with control over economic activity (the tax system, law enforcement agencies, and so forth). And this led to a conclusive removal of Russian administrators from this sphere.

Finally, during the decade that has elapsed since 1991, a new generation of Uzbek administrators has emerged, and it has a rather high professional preparation and educational level. As a result of their entry into the administrative apparatus, the demand for a “mobilized diaspora” decreased still further. The problem, however, is that many young, highly-qualified Uzbeks find administrative work unattractive because of the low salaries in such positions.

B. Change in the Language of Administrative Paperwork

Although a significant period of time has passed since Uzbekistan adopted the “Law on Language” (1989), William Fierman rightly points out that only the “symbolic part” of the law—associated with a change in the Russian-sounding names of streets, institutions, and the like—was most successfully applied.²³ Although some researchers regard this renaming as a partial revival of “a medieval lexicon,”²⁴ such renaming did not have a significant impact on the role of Russian language in the administrative apparatus.

With respect to transferring administrative paperwork to make use of the Uzbek language, the “Law on Language” was never implemented in a strict, systematic fashion. In part, this can be explained by the lack of material and technical resources, part of which, moreover, were diverted to support the conversion of Uzbek writing to the Latin alphabet. Moreover, computerization of the administrative apparatus proceeded in the absence of computer programs capable of working the Uzbek language and without the appropriately trained

²³W. Fierman, “Problems of Language Law Implementation in Uzbekistan,” *Nationalities Papers*, 23 (1995):592.

²⁴In the opinion of B. Sidikov, the process of renaming reflected the “spiritual and social structures typical for the middle ages. Here is an example: the former chairmen of the oblast executive committees began to be called ‘khokimiy’ (viceroys), the oblast executive committees became ‘khokimiiaty’, and the republic ministers became ‘vaziry’ (viziers). What changed was not only the name of the organs of governance, but—in a fundamental way—the very psychology of interrelations . . . within the component parts of power.” B. Sidikov, “Istoki sovremennoi religioznoi situatsii v Uzbekistane,” *Tsentral’naia Aziia i Kavkaz*, 5:11 (2000): 64.

operators and programmers. But there was a further factor at work here: “the Law on Language” of 1989 was adopted partly to reduce the pressure of the opposition (“Birlik” and others), which had actively exploited slogans about the revival of the national language.²⁵ In 1993-1994, the situation changed. The former opposition was removed from the political game; at the same time, the rapidly increasing exodus of Russians from Uzbekistan (compared to the late 1980s) had become a serious problem. Therefore, despite the fact that the original plans to review the “Law on Language” in 1992 had presupposed an “expansion of the sphere of the use of the national language,”²⁶ the new version of the law in 1995 was significantly milder with respect to the place of the Russian language in the administrative system. In particular, the new redaction excluded the demand that leaders and staff people speak the state language, a point contained in the law of 1989.

With time, the question about the exclusion of the Russian language from administrative documents has gradually ceded its original significance. Periodic verification of implementation of the law assumes the character of public campaigns (with treatment in the mass media), but such campaigns were short-lived. As a rule, no kind of administrative penalties was assessed from those who continued to conduct administrative work in Russian. Moreover, the appearance of a large number of foreign and international agencies in the large cities of Uzbekistan (where the overwhelming majority actively used Russian) also contributed to the preservation of the Russian language. Moreover, as a result of the improvement in relations with Russia in 1999-2000, informally the question was even raised about giving Russian the status of a second state language. However, the development of events after 11 September 2001 has had the effect of putting an end to such plans.

Nevertheless, from the beginning of the 1990s, there was a noticeable reduction in the spheres where Russian language was being used in administration. Russian continued to be used most extensively in the administrative apparatus of Tashkent and Tashkent Oblast, whereas in other areas (above all, in the Fergana Valley) it was already displaced in this sphere by the Uzbek language. A further factor is the continuing exodus of Russians (bearers of the literary norm of the

²⁵Calls to revive the national language were heard at meetings organized by the opposition in Tashkent on 3 December 1988 (at the university campus) and on 19 March 1989 (on Lenin Square).

²⁶“V Verkhovnom Sovete Uzbekistana nachata rabota po podgotovke izmenenii i dopolnenii v Zakon ‘O gosudarstvennom iazyke,’” *Kommercheskii vestnik*, 30 July 1992.

language) from Uzbekistan;²⁷ to that must be added the growing popularity of the English language. Therefore, the use of Russian as the de facto administrative language has lasted much longer than expected in the early 1990s; however, over the next decade Russian will in all probability be expunged from the lexicon of the administrative elites.

C. Change in Orientations

The question of excluding the pro-Russian orientation of the elites, in favor of one tilted toward the countries of the West, has its own special complexity. Notwithstanding the policy adopted at the beginning of the 1990s (a rapprochement with the West and the “semi-West,” Turkey), the orientation toward the earlier metropole among the administrative elites remained quite strong until the middle of the 1990s. In rejecting the transformation model of Yeltsin’s Russia (shock therapy, intensification in the parliamentary branch of power, and the like), the elites of Uzbekistan nevertheless preserved their former orientation toward Moscow. First, the earlier clientele ties with the Moscow elite were transformed into relations of business partners; that was further facilitated by the fact that the shadow economies of the two countries were legalized during this period and firmly linked with each other. Second, given the political instability in Russia during the first half of the 1990s, there remained the possibility that Russia would re-colonize Uzbekistan (in accordance with the “Tajik” or “Belorussian” scenarios); this potentiality also had an impact on the behavioral strategy of the Uzbek elites. Finally, despite the several large and widely publicized contracts with non-Russian companies from abroad, the role of foreign capital in this period remained too insignificant to offset the pro-Russian orientation that persisted in spite of the pro-Western political rhetoric. As an example one could cite the preparation of draft laws in the ministries and agencies of Uzbekistan during this period: the majority of them were compiled by using the text of this or that piece of Russian legislation. However, a similar practice becomes apparent if one analyzes the legal decrees of other Central Asian states.

²⁷According to some data, in 2000-2001 alone more than one million Russians legally emigrated from Uzbekistan to Russia; in addition, more than 15,000 people leave Uzbekistan each year without contacting the Russian embassy in Tashkent. “Migratsiia russkikh iz Tsentral’noi Azii rastet,” Radio Svoboda, 25 April 2002 (www.news.ferghana.ru/detail.php?id=244&code_phrase=).

In the second half of the 1990s, this orientation became significantly weaker, a process provoked by the strengthening of the elites' orientation toward the countries of the West—above all, the United States, along with Western Europe and an increasingly active Japan. Although the dependency on Russia did not decrease (according to some data, Uzbekistan's debt to Russia for state credits amounted to 617 million dollars in May 2001)²⁸ and, in strategic terms, actually increased in 1999-2000, the elites of Uzbekistan became more and more oriented toward the West. Tomorrow's generation of Uzbek administrators is studying in the universities of Europe and the United States; Western (above all, American) foundations are sponsoring various projects that provide financial and technical support for Uzbek administrative elites.

In this respect, the conclusion drawn by Russian experts is interesting (even if overtly utopian in their recommendations): "It is necessary to recognize that, in the states of Central Asia, an influential middle stratum of leaders has appeared, and that it is oriented in its values and preferences not toward Russia, but toward the United States, Iran (in the case of Tajikistan), and the European community, [and] less frequently toward Turkey, Saudi Arabia, and China. . . . Once a well-thought out Russian policy for the region has been prepared, it is essential to organize as a counterweight to this force on the pro-Russian part of the local administrative elite (which, in the countries of the region, is called 'pro-Soviet'). It is necessary to support openly those leaders of the second and third echelons of power who are more pro-Russian in their attitude than are their presidents. It is exceedingly important that interest in a close integration with Russia come not from Russian, but from local administrative elites."²⁹ Projecting this recommendation onto Uzbekistan, one can only guess precisely who it is that they propose to "support openly" as a counterforce to the "less pro-Russian" president. The sole grain of sense in the above passage is the sober confirmation of the accelerated de-Russification of elites and their rapid Westernization.

²⁸O. Solomonova, "Miach na rossiiskom pole," *Trud*, 5 May 2001.

²⁹V. I. Bushkov, I. V. Mazharov, and A. D. Sobianin, "Rossiia v Srednei Azii: kak preodolet' negativnye tendentsii" (www.cis.ng.ru/raiting/2001-01-31/6_aziy.html).

2. *The Westernization of Elites: The Role of the Western Presence*

In 1997, Bruce Parrott already noted the limits to Western influence on the process of Westernization in Central Asia, a tendency that he attributed to the following causal factors: “the greater geographical and cultural distance between the West and most of the non-European postcommunist states; the lower level of Western strategic interest in these countries, coupled with a tendency to manifest less concern about their internal liberalization than about their potential sources of energy and raw materials; the countries’ greater vulnerability to pressures from Russia preoccupied with ensuring the stability on its southern flank.”³⁰

Although these factors have not disappeared during the past five years, in my view they have nonetheless become less weighty. Above all, in the course of the antiterrorist campaign in Afghanistan, it proved possible to coordinate (at least, verbally) the political policy of Russia and the West with respect to Central Asia. The level of Western strategic interest in the region grew significantly. Moreover, there was also a parallel increase of interest in the liberalization of Uzbekistan: it has been precisely since 1997 that the country has realized the most significant projects to liberalize its system of administration. Furthermore, this interest is often transformed into direct political pressure, as in the case of resolution no. 397 adopted by the U.S. House of Representatives on 2 November 2000.³¹ But the initiatives to bring about a systematic revival of the Silk Route have significantly reduced the remoteness of the West from Central Asia as a whole and from Uzbekistan in particular. These initiatives include steps taken by the European Union since 1993 (the TRACECA [Transportation Corridor Europe - Caucasus - Asia] project), by Japan since 1997 (the “Eurasian diplomacy” of Ryutaro Hashimoto), and the United States since 1999 (the Silk Road Strategy Act)

It may well be that, of the causal factors cited by Parrott, the only one that is still operative is the cultural distance between the countries of the West and, in this case, Uzbekistan. First, however, it should be said that, strictly speaking, a difference of cultures has not always and everywhere served as a barrier to closer ties with the West. Second, in a certain respect (*viz.*, the almost complete

³⁰B. Parrott, “Perspectives on Postcommunist Democratization,” in: *Conflict, Cleavage, and Change in Central Asia and Caucasus*, ed. K. Davisha and B. Parrott (Cambridge: Cambridge University Press, 1997), 9.

³¹See E. V. Abdullaev, “‘Tsentral’noaziatskaia’ rezoliutsiia kongressa SShA (No. 397): politiko-pravovaia interpretatsiia,” *Tsentral’naia Aziia i Kavkaz*, 2001, No. 2(14).

secularization of the administrative system), the Uzbek ruling elites are rather close to their Western counterparts. Although the methods and means used to achieve this secularization and to exclude religious elites from power were illiberal and elicit criticism from Western organizations, the results of this process completely correspond to the notion of Westernization. Just as in the administrative apparatuses of countries in the West, in Uzbekistan religious affiliation is a private matter and has no direct influence on the process of governance. The contemporary administrative elite of Uzbekistan is secular; in the most fundamental way, this distinguishes it from the precolonial elite, which, as noted above, had a close alliance with the Islamic elite and used this alliance to augment its authority.

In general, after acquiring significant power since 1991, the administrative elites of Uzbekistan have avoided the need of sharing it with either religious or military (traditionally the most russified) elites. Indeed, right until the middle of the 1990s, neither the religious nor the military elites laid claim to power in any of the Central Asian states: many of the military officers were preoccupied with the “privatization” of the surplus weapons, while the majority of informal religious authorities lived quite well on the “grants” provided by various foreign religious centers. At the end of the 1990s, the situation in Uzbekistan did not sharply change in favor of either of these groups. The reinforced law-enforcement organs significantly outweighed the army in terms of significance and also launched a massive assault on the informal religious elites that were becoming active.

As a result of these processes, the administrative apparatus underwent an asymmetric increase in the role and weight of the law-enforcement organs, which—in the absence of earlier, “Soviet” counterweights in the form of a party apparatus and “red directors” of enterprises—turned into a kind of independent branch of power. Since in any society the law-enforcement organs constitute the most conservative element of the administrative system (given the specific character of their activity), the disproportionate concentration of power and influence in these organs has led to a distortion of the entire ruling apparatus and has retarded social development as a whole.

In this situation, the many initiatives in recent years to decentralize administrative power, to transfer part of its authority to local organs of self-

governance (*makhalli*), and the like have had an extremely insignificant impact on the real correlation of authority and power in the state. The administrative apparatus preserved its own rigid controlling and regulatory function with respect to the economy; given a situation of growing economic difficulties, it was even forced to increase its pressure on the economic sphere by resorting to various instruments of noneconomic coercion. This point, in the author's view, is the most vulnerable in the process of Westernization of elites, since it is precisely in questions of economic liberalization that one sees a "disconnect" with the interests of the West and Uzbekistan. "The doors are open to the West, but the West does not come in, because it is very difficult to work there"—such was the apt description provided by the radio journalist B. Abdullaev to characterize the situation with respect to the Western presence in Uzbekistan.³² In other words, in the case of Uzbekistan, the process of Westernization and, parallel to that, the growth of Western influence were limited not so much by geographic and cultural distance from the West as by the specific features of the transformation of the Uzbek administrative system. Nor can the distance from Russia be a significant factor; it suffices to note the significantly more Russian-oriented and yet more Westernized elites of Kazakhstan and Kyrgyzstan.

The intensification of contacts with the West and its influence in Uzbekistan that commenced after 11 September 2001 are qualitatively new, but that presence does not mark its first appearance. In the last decade, this is at least the third "wave" of Western presence in Uzbekistan. The first "wave" (which encompassed the years 1991-1995) was characterized, apart from the intensive establishment of diplomatic relations with Western countries, by an opening of numerous branches and offices of Western countries as well as by the influx of a large number of Christian missions from the West. In 1996-2000 there was a significant change in this "flow": because of the absence of a freely convertible currency, the number of Western companies decreased (leaving only the largest firms, such as Coca-Cola and Nestle); as a result of the ban on missionary activity, the number of foreign Christian missions contracted just as sharply. At the same time, precisely in this period Western organizations and foundations increased their activity in Uzbekistan, carrying out projects in the sphere of liberalization, human rights, and so forth. In this period too Uzbekistan intensified its military

³²Radio Svoboda, 24 May 2001 (www.uzland.uz/2001/may/27.htm).

cooperation with the United States and NATO.

The appearance of the Western military on the territory of Uzbekistan signified a new stage in the Western presence. It has been characterized by an intensification of military cooperation, economic engagement, and assistance for the liberalization of the economic and political climate (with the question of missionary churches, so far as the author knows, not being raised in this new context). With respect to the administrative system, this will signify the final reorientation toward the West. The new generation of Russian-speaking administrators of Uzbekistan (who began their careers after 1990) will be oriented toward the West, not Russia. Although the influence of the Russian language will be significant in the administrative sphere for a rather extended time to come, it will be actively displaced not only by Uzbek, but also by English. Moreover, the tendency to tighten the immigration rules in Russia (the main source of labor migration not only of Russian-speaking, but also indigenous inhabitants of Uzbekistan) is also, indirectly, eroding Russian influence (at the same time that, since October 2001, it became significantly easier for Uzbek citizens to obtain an American visa). Finally, one must also take into account the fact that the process of Westernization of elites is transpiring in Russia itself.

Within the framework of this article, it is possible to illuminate only certain aspects of the transformation of administrative elites in Uzbekistan. No attempt has been made here to examine the role of family and local ties in the formation of the administrative elites of Uzbekistan: as a result of the attractiveness of this subject for journalists and popular writers, this problem proved as mythologized as its significance has been exaggerated. In a situation where information about the details of personnel changes remains secret, an objective study of this subject is in effect impossible. There are also other “blind spots” in this essay (e.g., the relationship between central and regional administrative elites). Finally, it is as yet unclear how the new “wave” of Western presence in Uzbekistan will influence the situation in the country, and how effectively Tashkent will make use of the assistance provided by the United States. These and other questions must await further study.

The Question of Privatization in Azerbaijan and Georgia

Gubad Ibadoglu

The renaissance of the societies in Azerbaijan and Georgia, which took place amidst the collapse of the USSR, the establishment of independent, sovereign states, and the transition to market mechanisms of economic management—all this elevated the questions of property and ownership relations to an active level. The political transformations and revolutionary steps in the sphere of economic reforms throughout the post-Soviet realm have also augmented the potential vitality of the reforms undertaken in Azerbaijan and Georgia. The contemporary post-Soviet states of the South Caucasus also widely considered two other phenomena. One was the experience of restitution in the Baltic states, where some types of real estate were returned to former owners (the latter having been deprived of this property when these republics were absorbed into the USSR in the 1940s). The other was the rapid privatization reforms in Russia as well as similar developments elsewhere.

But these states in the South Caucasus, for a plethora of reasons, had to choose their own specific path of reform. Ever since the 1920s, all private property (even including housing in the urban areas and the livestock in the countryside) had been nationalized by the Soviet authorities and transformed into state property. That process effectively destroyed the class of property owners (of whatever magnitude—petty, middling, or large).

However, in the 1950s and 1960s, new forms of property relations had already begun to take shape. Specifically, the private territories of garden plots (constituted as rural household producers) appeared in rural areas, possessing their own livestock, private housing, and the like. Likewise in cities, mainly in those of middling and small size, productive, trade, and service institutions and shops in effect acquired their own owners in the person of their administrative heads and directors. These people invested their own personal funds (illegally, of course) in

order to expand production, make repairs, and the like.

These informal owners were the official heads of these enterprises, acting in the name of the state. And even with a change of management (for whatever reasons), the new leaders—after they had been officially confirmed in their new position—settled accounts with the former heads in a “purchase-and-sale” deal. These practices, although illegal, enjoyed de facto recognition from state authorities. Indeed, government officials participated in settling accounts with the results of these deals.

When the privatization of state property commenced in the 1990s, the property of the de facto (but not de jure) heads was also denationalized (“de-statified”). In accordance with the unwritten laws, in most cases it was the former head (or, with his consent, someone else) who became the legal owner. That is how the rules functioned—and these even enjoyed tacit recognition from the Soviet regime.

In the Soviet era, illegal heads ever more frequently succeeded in achieving higher indicators of economic efficiency than did the larger state enterprises. Moreover, once these “non-state” enterprises had fulfilled their state production plan, they worked for themselves, thereby generating the “shadow sector” of the socialist economy.

Hence private ownership of land and property had firmly taken root in Azerbaijan and Georgia, and thus the introduction of privatization did not meet with resistance. A significant part of the contemporary entrepreneurs in Georgia and Azerbaijan went through this school of “shadow business” in the USSR and mastered the specific rules of working under such conditions.

Privatization in Georgia

The Process

The wave of privatization swept across the post-Soviet countries of the South Caucasus from the beginning of the 1990s. The first to move in the direction of privatization was the government of Georgia. It initiated its program to privatize state property and to establish new forms of property and management,

but it did so under extremely difficult economic and social conditions. At the present time, it is now bringing this process to completion.

The privatization itself began in Georgia in 1993. However, under the conditions that then prevailed (viz., amidst the conflict in Abkhaziiia), it was difficult to conduct an effective economic policy. In addition, like the other former Soviet republics, Georgia proved to be unprepared for the transition to a market system. Nor did it possess a full-fledged legal foundation for privatization. Hence it was with extreme difficulty and slowness that it proceeded with making such a large-scale transformation in the economic, political, social, and legal system. Nevertheless, in spite of all these difficulties, Georgia proceeded to launch the process of privatizing state property. Simultaneously, the government worked out a strategy for future steps of denationalization, then devised the methods for carrying this out, and approved the legislative basis for this process.¹

Chronologically, three basic stages can be discerned in the process of privatizing state property in the Georgian Republic. In the first stage (1991-1993) the government laid the legislative foundations for denationalization and privatization, established the corresponding infrastructure, drafted the methodological documents, and acquired practical skills. To create the basic legal framework for the privatization process, the government adopted laws on the right of property ownership, entrepreneurship, antimonopolistic activities and unfair competition, support of investment activity, leasing and lease relationships, ownership of agricultural assets, protection of consumers' rights, and a number of other legal documents. All these were intended to bring order into the sphere of privatization and, more generally, in the legal framework for property relations.

Nevertheless, with respect to adopting concrete measures to privatize state property, the legislative base was virtually nonexistent, for at the outset of this process the Georgian Republic possessed only a few legislative documents. It adopted its first program of privatization on 11 August 1992. In practical terms, the process of privatization in Georgia actually commenced in March 1993, but the compilation of inventories of state property was based on the situation on 1 April.

During this first period, the government laid the main emphasis on the privatization of enterprises in trade, public catering, and services. As in many other countries, privatization began with small economic units. According to official

¹Emir Dzhugeli and Iraklii Gvaramadze, "Transformatsiia form sobstvennosti v Gruzii," *Tsentrāl'naia Aziia i Kavkaz*, 1999, no. 4.

statistics, between 1993 and 1998 the state privatized 12,860 small enterprises, and with that the “small privatization” was generally complete.

Of the total number of privatized enterprises, those involved in trade accounted for 36.6 percent. Enterprises in the service sphere represented 43.5 percent of the privatized entities. The balance included enterprises in industry (2.2 percent), transportation (0.9 percent), energy (0.3 percent), and agriculture (3.7 percent).

At the present time, the level of privatization in trade and public catering stands at 90 percent. The sphere of services has been almost entirely privatized. In this period, the state also initiated the denationalization of small and medium-sized enterprises in industry, agriculture, construction, and other branches.

To involve the broad masses of the population in the process of denationalization and privatization, in 1993 Georgia began to implement a program of mass privatization. This mass privatization was carried out with the assistance of specialized voucher and monetary auctions. In addition to these instruments, the state conducted direct sales of controlling shares of stock and held commercial competitions.

Apparently, the goals of the Georgian “voucher program” were primarily political, and only secondarily did they pursue the goal of a systemic transformation. Thus one of the principal goals of the Georgian program was not only the rapid denationalization and privatization of all sectors of the economy, but also the formation of diversified forms of property. It was also assumed that the process of privatization should by itself stimulate the formation of self-regulating market mechanisms, and that these in turn would transform the social psychology of the majority of the population.

The main goal of the privatization policy in the second stage was to transform the large and middle-sized enterprises in industry, transportation, and construction. Moreover, the policy took into account the specific peculiarities of each branch, the need to reorient production toward new markets, and the establishment of new economic relationships with suppliers and closely related firms. The privatization of medium and large state enterprises in Georgia began with their transformation into joint-stock companies.

With the adoption of the Program of Denationalization and Privatization

in 1997, Georgia entered the third stage of privatization. In this phase the government of the Georgian Republic began the denationalization and privatization of enterprises in fundamental, strategically important branches of the economy: energy and telecommunications. The special feature of this stage predetermined a change in strategy and the tactics of privatization. Namely, the government slowed the rate of privatization, employed an individualized approach, and shifted to a selective method of privatization (based on a complex analysis of the financial condition of enterprises; their significance in the economy of the republic; the financial restructuring of enterprises; technological upgrading and reconstruction of production; and the attraction of large-scale investments from strategic investors).

By the beginning of 1997, it had become clear that the methods of stabilization being applied had proved to be insufficiently effective to bring this stage of the transformation of property to a successful conclusion. Instead, it was necessary to apply more decisive measures to accelerate the process of privatization, which had been too slow and drawn out.

As a result, the government of Georgia, with the goal of transferring state-owned stock to private hands, on 27 June 1997 adopted a decision to conduct specialized auctions. Subsequently, these auctions significantly accelerated the process of privatization. Here it is necessary to point out that this method was the most effective form of privatization in Georgia.

To accelerate the process of privatization, and on the basis of advice by the World Bank, Georgia has conducted two specialized “zero reserve price auctions.” These auctions were the most effective when compared with other methods: these two auctions sold almost a third of the entire number of stocks that have been sold.²

Today, almost all the small enterprises are in the private sector, while a significant part of the large enterprises remain in the state sector. For example, the state owns 78.3 percent of the stock in the Kutaisi Automotive Plant. The flagman of the Georgian economy in Soviet times—the Rustavi Metallurgical Complex—was completely shut down a few years ago. There is now an active search to find an investor to take over this enterprise.

A more successful example of the change in ownership was the Rustavi

²Emir Dzhugeli and Iraklii Gvaramadze, “Nulevye’ auktsiony: tseli i analiz rezul’tatov,” *Case* (Warsaw), no. 140, September 1998 (www.case.com.pl).

enterprise “Azot,” which resumed operations with the participation of Russian and Georgian investors.

Privatization in energy began in 1998. The American AES Corporation acquired 75 percent of the stock in the joint-stock company Telasi (Tbilisi Electric Power Grid). In 2000, this company acquired two of the most powerful energy blocks in the Tbilisi district power system and took over the management of two hydroelectric power stations. In 1996 Georgia began the process of privatizing the national communications firm Geocell through the creation of a joint-venture enterprise, with the Turkish firm Gurtcell possessing the controlling share of stock. But perhaps the most successful privatization of all was in the food-processing industry, which has virtually no state enterprises and which has actively attracted investment. In general, the lion’s share of investments have gone to the transit system of the country to finance the modernization and construction of the transportation infrastructure (in particular, for the construction of new oil and natural gas pipelines).

Among the foreign investors are representatives from forty countries in Europe, the Americas, and Asia. The largest investments have come from Israel (18,079,511 U.S. dollars), Ireland (17,917,530 dollars), Turkey (11,968,420 dollars), Great Britain (11,480,683 dollars), the United States (11,480,683 dollars), South Korea (9,120,500 dollars), and Germany (8,818,206 dollars).³

In 1997, the total volume of investments amounted to 120,822, 106 U.S. dollars. The greatest volume of investments went into industry (35.81 percent) and communications (25.19 percent).

In the course of 1992-1993, Georgia privatized 60 percent of the agricultural land in the country. At an early stage in this process, it also conducted the privatization of state apartments on gratis terms. Altogether, at this point, the country has privatized approximately 12,000 small entities and more than 1,100 medium and large enterprises. Hundreds of thousands of Georgian citizens have become property owners. In contrast to many countries in the Commonwealth of Independent States (CIS), including Azerbaijan, the privatization of medium enterprises in Georgia was conducted such that, in compliance with a decree by the president of Georgia, they all were transformed into joint-stock companies in which 50 percent of the stock was transferred to the collective of employees.

³For the various data and statutes, see: <http://www.georgia-gateway.org>.

The quantitative indicators for privatization (per form and branch) are presented in Table 10-1.

Table 10-1
Privatization in Georgia (1993-1999)

Branch	Tender	Auction	Direct Sale to Juridical Entity	Direct Sale to Private Individual	Lease with redemption	Liquidation	Joint-Stock Company
Industry	29	51	41	0	42	91	243
State Sector	11	4	12	0	4	2	91
Grain and its Products	0	5	52	2	40	0	24
Agriculture	76	158	52	0	103	89	326
Construction	127	88	19	0	19	28	212
Trade	1393	1232	1030	0	697	373	70
Public services	1458	1778	631	0	742	985	
Oil products	48	110	7	0	1	0	26
Health	53	50	415	0	9	25	
Social services	144	164	168	7	45	31	42
Transportation	23	26	310	0	26	12	110
TOTAL	3362	3667	2458	9	1728	1636	1144

Conclusions and Predictions

The methods and forms of privatization applied in Georgia were characterized by their heterogeneity. Along with the tested methods of small and mass privatization that was based on the use of vouchers, Georgia also utilized the method of selling stocks at specialized monetary auctions. The special character of the latter consists in the involvement of a large circle of investors without limits on the number of participants. The experience gained from conducting the special monetary auctions, to a certain degree, suggested the idea of “zero auctions,” which were the most effective and fastest method for privatizing state property.

The former Minister of Economy of Georgia, V. Papava, has offered the following opinion: “If investments in the requisite scale do not appear, then the dead enterprises will move from the state to private hands. Moreover, they will fall into poor hands. But this will lead to a stagnation in production, to the expiration of industry, and that obviously weakens the potential of the economy and has a devastating impact on the state budget and on the budget of every family.

Unfortunately, that has been the result of privatization. With respect to the vouchers, their owners sold these at a price six times below their value. Thus the formation of a class of property-owners with the assistance of the voucher system, as practice has shown, proved to be a self-deception. Nor can there be any question but privatization was accompanied by fundamental corruption.”⁴

It is also necessary to note that many enterprises in Georgia produced goods for the enormous market of the USSR and other countries in the socialist bloc. And that required the creation of large productive capacities. Today, to satisfy the needs of Georgia, such capacities are not needed, especially since their condition leaves much to be desired. The process of privatization can accelerate the tempo of structural upgrading of enterprises and their adaptation to a market system. Of course, this entails the reorientation of production at many enterprises, but it also requires the declaration of bankruptcy at some of them. However, the more quickly this process is completed, the quicker there will emerge a healthy structure of production that is adapted to the constantly changing market conditions. Simultaneously, there will be a deregulation of the economy.⁵

The present result of the process of mass privatization can in general be evaluated on the basis of world experience from various approaches:

- political goals (involvement of a broad circle of the population in the transformation processes);
- social goals (application of fair principles in the distribution of shares of stock);
- systemic goals (establishment of market mechanisms in the economy);
- efficiency goals (improvement of the effectiveness of the operation of enterprises).⁶

The majority of countries that have carried out privatization have set for themselves goals, some of which are not mutually related. In Georgia, an important, if not top-priority, goal of privatization was political. It was thought that each citizen, having received a voucher (which could be turned into the stock of privatized enterprises) would feel themselves co-participants in a constantly functioning private sector of the economy.

⁴*Nezavisimaia gazeta*, no. 82 (2392), 11 May 2001.

⁵V. Pan'kuv and B. Gonchazh, "Privatizatsiia za liubuiu tsenu. Analiz opyta Republiki Gruzii v 1997-1998 godakh," *Case* no. 141, October 1998 (<http://www.case.com.pl>).

⁶V. Ermakovich, "Modeli privatizatsii," *Case*, no. 104 (<http://www.case.com.pl>).

But the final result of privatization was far removed from what had been envisaged. The population felt that it had been deceived. The vouchers, in theory, were to be exchanged for the stock of privatized enterprises. However, this procedure was new and unfamiliar for the majority of citizens, who had not heard about stocks and corporate deals. They could not understand why, after decades of a life that entailed sacrifice, war, and industrial growth, their individual share in the wealth of the country was a miserably small amount, or more precisely worth next to nothing. Such was the case in spite of the fact that the voucher indicated an amount in the national currency equivalent to 30 US dollars.

Thus, the political results of privatization proved unexpected. On the one hand, the broad masses of the population were involved in the voucher process, but they did not become stockholders and co-owners. And instead of giving birth to a new class of a national petite bourgeoisie, there emerged a small coterie of people from government circles who, for all practical purposes, had concentrated all the wealth of the country in their own hands. And next to them was an army of disillusioned and impoverished people.

The social results of privatization were also uneven. They are the product of what has been described above. People, having heard broken and incoherent promises about stocks, dividends, and a happy life, discovered that the stocks do not yield dividends. Indeed that life of happiness proved more remote than it was in the USSR, because the new post-Soviet government guarantees them absolutely nothing.

As for what was attained with respect to systemic goals (that is, an absence of price controls, the development of private property, and the promotion of competition), here certain gains were achieved. Thus, private property did in fact appear, the prices did actually become free, and competition often did arise.

However, it must be noted that, in reality, a class of property owners did not emerge as a result of privatization. In the majority of cases, the former Soviet “shadow owners” legalized “their” property by using the vouchers and by buying them for next to nothing from the people in their employ.

Competition is often conducted in a dishonest fashion. Perhaps these are the excesses of a “young” market system, but in our view it is precisely in this sphere that the business norms for the future are being formulated. And such a

tendency is dangerous.

According to expert calculations, in 2000 the private sector accounted for 68 to 70 percent of all output and had 60 percent of the fixed capital. In the fuel and energy, metallurgical, and petrochemical industries the share of private ownership accounted for 40 percent of the output and 45 percent of the fixed capital. The corresponding indicators (percent of total output and percent of fixed capital) were 70 and 65 percent for machine-building, 95 and 85 percent for construction materials, light industry, and food-processing industry, 85 and 75 percent for construction, 95 and 85 percent for agriculture, 40 and 40 percent for both indicators in rail and sea transport, 65 and 70 percent for air transport, 90 and 85 percent for motor vehicle transport, 30 and 25 percent for communications, 90 and 85 percent for trade and public catering, 100 and 100 percent for public utilities and services, and 50 and 60 percent in other spheres.⁷

As for official prognoses about the future, the Georgian government has recently approved a strategy for the privatization of state property until the year 2003. This program foresees, in particular, transferring to investors the controlling bloc of shares in huge enterprises in the spheres of energy, industry, construction, transportation, communications, public health, and education. The minister in charge of state property, M. Ukleba, declared that “by the end of the current year privatization of productive associations in Georgia is to reach eight electric power distribution companies, but also five hydroelectric power stations (in the western part of the country and now owned by the state).”

The agenda for today includes the privatization of telecommunications and ports. At the forefront is the privatization through international tenders, with the participation of foreign investors.

Azerbaijan

Process of Privatization

In Azerbaijan, the first phase of transforming property relations began at the end of 1995. Although the government body in charge of privatization had been established in 1992, the “Law on Privatization” was not adopted until January

⁷For various data, see <http://www.georgia-gateway.org>.

1993. The delay in privatization played a decisive role in the squandering and pilfering of state property and in the cessation of operations at a quite significant number of the enterprises. During this period, Azerbaijan lost 62 percent of its gross domestic product (GDP), and the standard of living of its people plunged by a factor of four.

The official, so-called “small” privatization began at the end of March 1995. The distribution of privatization shares (vouchers) began in March 1997, and the privatization of medium-sized enterprises commenced in May 1997.⁸

However, the mass privatization has until now still not been completed. The process of privatization was suspended in 1999—for the most part, because of subjective reasons. The outbreak of a conflict of interests within the higher echelons of power became a brake on the privatization process. The contradictions between the adherents of privatization by check and those favoring a monetary privatization were the main reason for this halt in privatization. The interests of the “check” group were directly linked with their obligations to foreign investors and those who owned vouchers and options (in the amount of 450 million US dollars). These checks were intended for the privatization of Gosneft’kompaniia (the State Oil Company). As a result of the resolution of disputes in favor of the “monetary” group and the exclusion of the check group from the process of privatization, foreign investors began to file accusations against the government of Azerbaijan. Minister of Economic Development, F. Aliev, declared the following: “I understand that this is a subject of concern for foreign investors. Because of a certain interest in strategic enterprises (for example, the State Oil Company of the Azerbaijani Republic), some foreign investors exploited the advantage of this system. They bought vouchers at a very low price from Azerbaijani citizens, who had received the vouchers gratis.”⁹

From the beginning of privatization, this process privatized 31,226 small entities and enterprises, 9.9 percent of which were bought by the employees themselves. Of the total enterprises privatized, 9,421 were in the service sphere, 14,376 in transportation, 2,906 in trade and public catering, 605 in industry, 567 in the cereals trade and bakeries, 514 in motor vehicle services, 261 in construction, 255 were state enterprises under lease arrangements, 81 had

⁸G. Ibadoglu and E. Alibekov, “Privatizatsiia v Azerbaidzhane,” *Case*, no. 163, March 1999 (<http://www.case.com.pl>).

⁹Ministry of State Property in Azerbaijan (<http://www.msp.gov.az>).

suspended construction, and more than 100 were pharmacies and other entities. For the period 1995-2001, the government obtained approximately 46000 billion manat (95 million US dollars) in revenues from privatization.

If one analyzes the privatization on the basis of qualitative indicators, then the government did not attain its formal, officially announced goals: involving the broad mass of the population in the process of economic transformation, and ensuring social justice in the distribution of stock shares. At the same time, the fate of the majority of privatized enterprises proved pitiable, and at the present time many of them are no longer operating.

According to statistical data, after privatization the volume of production fell fivefold in the ten enterprises of a former state trade-industrial concern, fourfold in fourteen enterprises from the state concern "Azerbaijani Food-Processing Industry" (Azpishcheprom), and twofold in twenty enterprises in the state concern "Consumer Goods." Of ninety broiler plants (with an aggregate annual capacity of producing 60,000 tons of processed chicken), today only nine or ten plants are still operating.¹⁰

On 1 January 1999, the total number of shareholders who had participated in the privatization process amounted to 60,721 people—that is, less than 1 percent of the population of Azerbaijan. The same indicator stood at 60 percent in Poland and 56 percent in the Czech Republic. The passivity of the population of Azerbaijan was due to the fact that the State Committee on Property created various artificial barriers to the population in the course of privatization. Another cause was the lack of rank-and-file citizens with primary capital. Moreover, the lack of transparency in the process and the weakness of public control did not permit ordinary people to gain benefits from participation in privatization. Therefore citizens prefer to sell their own privatization shares (vouchers) to any buyer rather than themselves personally invest in a concrete enterprise.

The situation was intensified by the interruption of auctions at the beginning of 1999. This only delayed the process of creating new shareholders from ordinary citizens. During this time, moreover, a certain part of the shareholders sold their "petty" shares.

It should be noted that, whereas in 1997 the government held 14 check

¹⁰G. Ibadoglu (Bairamov), "Privatizatsiia v Azeбайдzhane: itogi i perspektivy," *Sbornik nauchnykh statei*, 30 (Kiev: Institute MEMO NAN, 2001).

and just as many monetary auctions, in 1998 it conducted 22 check and 26 monetary auctions, in 1999-2000 it organized only 5 check and 7 monetary auctions. The slowdown in holding check and monetary auctions not only limited the opportunities for ordinary citizens to become shareholders of privatized enterprises, but also dealt financial harm to the investment groups that held a significant volume of privatization shares and options. Unfortunately, such treatment of foreign investors formed a negative image of Azerbaijan in the eyes of investors and creditors.¹¹

As for the consistency of the stages, then one of the most important—namely, the creation of check investment funds—was not at all realized in Azerbaijan. For purposes of comparison, the program of mass privatization created 660 such investment funds in Russia, 429 in the Czech Republic, 89 in Kazakhstan, and 15 in Poland.¹²

In Azerbaijan the absence of investment funds led to the destruction of the balance between demand and supply in the stock of the privatized enterprises. As a result, the population took a wait-and-see position and, as a result, used only 18 percent of the privatization checks during the first stage of privatization. By contrast, this indicator stood at 56 percent in the Czech Republic, 59 percent in Poland, and over 90 percent in Georgia and Kyrgyzstan. Privatization did not contribute to a reduction in unemployment but, on the contrary, the shutdowns of enterprises caused the number of unemployed it to increase.

Finally, after a long discussion, on 10 August 2000 the government adopted the State Program for the Privatization of State Property, thereby inaugurating a new stage in the privatization process. The mechanism of the second program of privatization in Azerbaijan was mainly constructed on the principles of the Russian privatization program from 1 July 1994. That was the case in spite of the fact that the models of privatization in these countries were different. At the same time, the second program was not free of all the shortcomings and unwarranted elements in the first program. As a result, there is no hope that the realization of the second program of privatization will serve to improve the general economic and financial situation in Azerbaijan.

¹¹G. Ibadoglu (Bairamov), "Privatizatsiia na Vostoke," *Case*, no. 225, April 2001 (<http://www.case.com.pl>).

¹²G. Bayramov, "Privatization in Azerbaijan: Analysis in Comparison with the Experience of Foreign Countries" in: *Azerbaijan Today*, August-September (<http://www.azerbaijantoday.az>).

Conclusions and Prognoses

The deteriorating position of privatized enterprises can be explained by several factors.

First, the majority of these enterprises suffer from an acute shortage of financial means. The lack of a corresponding capital market in Azerbaijan, together with the inefficient issue of credits, have made it difficult to attract additional resources to enable these enterprises to function. The situation is further aggravated by the heavy tax burden on the productive branches and by the problem of nonpayments. It should be noted that the mistakes committed in the process of privatization have become a serious obstacle to the subsequent development of the privatized enterprises. In the first instance, entrepreneurs who acquired controlling blocs of stock in enterprises in the course of the preferential subscription for employees and at check auctions have taken no interest in the monetary auctions. Therefore at many enterprises monetary auctions did not take place. As a result, the process of restructuring these enterprises has been delayed.¹³

Second, the process of privatization in the republic was conducted according to a single scenario that failed to take into account the specifics of a given branch. That has led to significant losses and contractions in the sphere of production. For example, in the agrarian sector the technological chain has been disrupted. Namely, at the point when they began to distribute gratis land allotments to private owners, there was no parallel privatization of processing plants and other production entities. For example, in viticulture, the peasants did not have the opportunity to sell their harvest for processing and, as a result, have destroyed their vineyards and instead have planted mainly cereals on their land.

At the same time, privatization in this sector was conducted simultaneously in Ukraine, Kazakhstan, and Russia. Moreover, in these countries a portion of the shares of the enterprises were redistributed at preferential prices among the producers of agricultural products. As a result, this process served more to link the producers and processors and to bind their interests together.

One other problem, which arose because of the lack of a normal program for the rehabilitation and renewal of privatized enterprises, had the effect of placing part of the enterprises in the hands of owners who did not intend to become occupied with the enterprise and its activities. After making a small “cosmetic”

¹³G. Ibadoglu, “Protsess razgoudarstvleniia sobstvennosti nuzhdaetsia v tselenapravlennoi politike,” *Consulting and Business*, 20001, no. 1: 58-62 (<http://www.consulting.azeri.com>).

repair of the enterprises, they attempted to resell it to other, larger investors at a higher price. They did not have sufficient capital to make the necessary investments, and the windfall from the difference the purchase and sales price was perfectly satisfactory as far as they were concerned.

All this leads to a slowdown in the tempo of economic development of the country as a whole.

As a result, privatization in Azerbaijan has encountered numerous problems of a political, economic, and social character. There are many causes for the above results. Among these one could cite the following:

- problems associated with the essence of the current regime, which seeks to divide all state property in favor of a small circle of people;
- the weak trust of general population for state authorities;
- the high level of corruption;
- the incomplete system for forming joint-stock companies and inadequate mechanisms of privatization;
- the lack of a market methodology to assess the property of privatized enterprises;
- the shortage of financial means among the population to realize a successful privatization, and also the lack of direct access to the international market of capital to attract foreign investments;
- the lack of check investment funds;
- the failure to conduct informational, explanatory work among the general population;
- the lack of conditions for parliamentary and public control, and hence the absence of the necessary transparency for the results of privatization.

As a result, privatization has been ineffective if judged in terms of economic, social, and other parameters. Therefore a significant part of the population of Azerbaijan is dissatisfied with the results of the first privatization program. The result of privatization as conducted in Azerbaijan was not consistent with the main goals of the privatization program; nor was it compatible with the

fundamental ideas and values of a democratic society.¹⁴

Among part of the population, as before, ideas of a “revolutionary character” are circulating. Sometimes people express ideas about the need to reexamine the results of privatization and to redistribute this property. Such proposals cannot fail to elicit alarm from authorities as well as investors.

Now, seven years later, we can confirm that precisely the opposite to those goals has been the outcome. Namely, there has been an improvement (and on a massive scale), but only for a numerically insignificant group—viz., for the former *nomenklatura* that lived well under the Soviet regime, for the still smaller group of *nouveaux riches* that now constitute the elite of post-Soviet Azerbaijani society. Moreover, the enrichment of this elite occurred, as in other post-Soviet states, at the expense of the budget of the country, and also the “shadow sector.” And the condition of the mass of the population has sharply deteriorated. Obviously, this process of enrichment of the rich and the impoverishment of the poor became possible because Azerbaijan, like other post-Soviet republics, acquired an authoritarian system of rule that relied upon the former *nomenklatura*, whose authority was not under real control by the people. Naturally, when the market reforms and privatization were realized with a regime that operated independently of popular control, these processes were inevitably bound to serve, first and foremost, the interests of these authorities.¹⁵

Thus the course of privatization in Azerbaijan had the effect of establishing a model of “monopolistic-*nomenklatura* capitalism of a clannish variety.”¹⁶

Privatization has accelerated the process of market formation. However, at the same time, the reform of relations in property created and limited the formation of normal market forces.

Therefore, under conditions of realizing the existing model for the transformation of property relations, the mechanism of privatization redistributed the national resources of Azerbaijan at the expense of the economic progress of the country. The private sector is being formed mainly as a shadow sector of the

¹⁴G. Bayramov, “Privatization in Azerbaijan: Results and Prospects,” *Central Asia and the Caucasus* [private informational and analytical journal, Sweden], no. 4(10), 2001 (see <http://www.ca-c.org>).

¹⁵G. Ibadoglu, *Izderzhki “perekhodnogo perioda” v Azerbaïdzhana* (Moscow: Letnii sad, 2001); see <http://www.sakharov-center.ru>.

¹⁶A. Masimov, “Privatizatsiia v Azerbaïdzhane: realii, problemy, perspektivy,” *Tsentral’naia Aziia i Kavkaz*, 1999, no. 4.

economy. In recent years, the proportion of the shadow sector in the GDP has steadily increased. In 2001, the sector accounted for 71 percent of the GDP (see Table 10-2).

Table 10-2
State and Private Shares of the Gross National Product in Azerbaijan

Sector	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001
Private	15	17.7	24	29.3	34	38	46	55	62	68	71
State	85	82.3	76	70.7	66	62	54	45	38	32	29

Source: *Ekonomiceskii obzor Azerbaidzhane* (Biulleten' TASIS, Goskomstat Azerbaidzhana).

As for the government forecasts about the future, it has recently made objects of strategic significance available for privatization. These include enterprises and production complexes in the chemical, machine-building, fuel-and-energy industry, branches of communication and air transport, and so forth. Privatization of these enterprises in accordance with the second program will be realized by holding investment competitions and on the basis of individual projects.

Conclusions

Privatization is a complicated process, one that is determined by a multitude of factors, objective and subjective, at the macro and micro levels. At the macro level, a major role is played by the government's economic policy, its practices in the management of economic processes, and the economic condition of individual branches and the country as a whole. At the micro level, the course of privatization depends on the mentality, goals, and directives of the main actors. It also depends on the organized structures and groups of influence, the specifics of the economic condition of a given firm, its organizational and production structure, the relations with other enterprises and "higher organs," and so forth.

From the above it follows that privatization must not be reduced to a formal transfer of property rights by the state, but should contribute to the

formation of new relations, when the microeconomic decisions are taken in the interests of a personified property-owner. Many post-Soviet countries, including Azerbaijan and Georgia, in reality support a policy of “privatize now, regulate later.”

A change in the system of management and control over enterprises, along with assistance in the development of new management, should contribute to a change in the behavior of enterprises under the new conditions. The restructuring of privatized enterprises and the renewal of enterprises after privatization must be conducted simultaneously with an improvement in the economic system of the country as a whole.

There are two obstacles must be overcome for this process to move forward.

First, it is essential to create the institutionalized conditions needed for the development of a new system of cooperative management at enterprises. The key factor here is the construction of organizational-legal frameworks for the operation of enterprises. In developed capitalist countries, economic entities are formed with the goal of ensuring the most effective operation of the firm in the market and hence the fullest realization of the interests of the owner. The codification of organizational structures and the methods of constructing them in these countries represented, to a certain degree, making the most effective decisions from what already then existed. In post-socialist countries such decisions could not spontaneously arise, because the transformation of the economy (in particular, privatization) signifies a conscious, managed process of changing one set of principles for the functioning of economic entities with entirely different ones. It is therefore necessary to introduce laws and the practice of relations between the state and enterprises.

In this regard, the problem of choosing an ideal institutional model becomes a top priority. It is toward this objective that reformers must strive and find ways to construct such a model.¹⁷

Second, a no less important barrier is linked to the fact that, in the event of privatization of state enterprises, the structure of administration and control must be transformed, not constructed *ab ovo*. The privatized enterprise inherits from its statist hypostasis the old connections, the hierarchy of influence of various

¹⁷J. Erle and S. Estrin, “After Voucher Privatization: The Structure of Corporate Ownership in the Russian Manufacturing Industry,” Site Working Paper No. 120 (Stockholm: Stockholm Institute of Transition Economies and East European Economies, 1997).

groups, traditions, experience, and mentality. Therefore the construction of new structures and relations can differ significantly from what reformers at the top had conceived and intended. Experience shows that, in many post-socialist countries, the success of such construction depends on how successful the new property owner is formed, to what degree the enterprises develop relations that are based on the factor of ownership.

Azerbaijan and Georgia did attain their political and systemic goals, but not their social objectives and overall effectiveness. The experience of Azerbaijan and Georgia shows the advantages of a more moderate, in contrast to mass, privatization. The rapid process in these former Soviet republics during the first stage, when its mechanism were not clearly designed, resulted in the bankruptcy of many privatized enterprises, and that in turn precipitated a growth of unemployment.

The realization of mass privatization in various countries shows that voucher privatization is a very complex process in a technical and organizational sense. Although these programs do not have a political alternative, it must be emphasized that they are not always economically successful. And if there is an opportunity to abandon this model, it is essential to do so.

Summing up the practical questions of privatization in Azerbaijan and Georgia, it is possible to say that in both countries the results of privatization were very similar in terms of achieving political, social, and economic goals. Both countries are governed by a group of people who passed through the same school and who belonged to the former Soviet party *nomenklatura*. And although rhetorically they invoke market categories, in essence how they make decisions and realize them remain just as they were before.

As a result of the action of these or other factors, which are associated with the struggle for political and economic power, Georgia and Azerbaijan have given rise to the syndrome of “unfinished privatization.”

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