FOREIGN TRADE OF THE CENTRAL ASIAN REPUBLICS 1992-2004

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DECLARATION

I declare that the dissertation entitled, **"FOREIGN TRADE OF THE CENTRAL ASIAN REPUBLIC 1992-2004"** submitted by me for the award of the degree of Master of Philosophy of Jawaharlal Nehru University is my own work. The dissertation has not been submitted for any other degree of this university or any other university.

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CERTIFICATE

We recommend that this dissertation be placed before the examiners for the evaluation.

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Dedicated to my adorable Father
Ranjit Kanta Roy Chowdhury
and mother
Meera Roy Chowdhury

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PREFACE

After the disintegration of Soviet Union the five Central Asian economies are moving from centrally planned economy to market based economy .they are in a period of transition. These five countries are undergoing political social and economic transformation. Success of these state will depend on the economic reform pursued by them .It is essential for these economy to diversify and open their economy, in order to promote their foreign trade.

Promotion of Foreign trade is beneficial to every country of the world. Many theories argue this view. This is the theme which is discussed in first chapter. In first chapter contending theories of foreign trade have been discussed.

Second chapter discusses the problems and issues in terms of choosing policies to promote foreign trade .Various alternative path is available to each of the central Asian economies as they are faced with the dilemmas in making an appropriate and rational choice . Among many dilemmas one of the prominent is the choice between regionalism versus multilateralism. Second chapter also discusses the obstacles in opening of the external sector.

Third chapter discusses the Foreign Trade structure and Foreign Trade Regime in each of the five central Asian economies. It analyzes the causes of particular type of foreign trade structure and regime prevailing in particular Central Asian countries. At the same time it also studies the impact of such trade regime and structure on the economy of the Central Asian countries. Taking into account the globalization and multilateral trading regime an attempt has been made to discuss the economic reforms in Central Asian economies with respect to issue of membership of WTO for these countries.

Fourth chapter concludes the study taking a realistic view of economic reforms in Central Asia .It highlights challenges as well as the potential of the region. It also provides tentative solution for the promotion and diversification of Foreign Trade.

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THEORY

CHAPTER 1

THEORY

WHY COUNTRIES TRADE

International trade has the potential to bring the poor countries out of its poverty. Poor nations have witness, how rich nations have increased their wealth by trading with each others. For resource poor country the trade provides an opportunity to earn more in richer markets and gain more resources to fight poverty and unemployment. Trade gives the peasant economy an opportunity to diversify the economy and meet the growing glamour for jobs.

Though the returns from international trade to raw commodity producing country are low, but it is of great importance for the development efforts. This is the reason that in spite of the drawbacks LDC[1]s stays in the system.

The international trade has been going on for thousand of years and its reference has been found in some of the earliest books of the bible. An international trading transaction takes place because some one in one country has something that someone in another country wants to buy. It is very rare that any country can produce everything, for example, Britain does not have the climate to grow coffee or tea, where as Kenya has the climate. An international exchange allows British people to enjoy coffee and tea. At the same time Kenyans to have the foreign currency to buy other goods in the international markets. Climatic

[1] A country with less advanced technology and/or lower income levels than the advanced industrial countries. Most LDCs have high dependence on primary sectors in their production, and more so in their external trade. Most have low average incomes, though a few of the smaller oil exporters, such as Kuwait, have per capita incomes comparable to those in industrial countries. Being an LDC is a mater of degree. Many countries in Sub-Saharan Africa are LDCs on any possible criterion, but many of the newly industrialized countries (NICs) such as China have a mixture of very poor primary producing sectors and more advanced industry. Members of the organization for Economic Cooperation and Development (OECD) are not classed as LDCs, although Turkey, which is a member, has a lower per capital income than some NICs. The former planned economies of the ex-USSR and Eastern Europe present similar problems of classification. Tajikistan is clearly an LDC, whereas the Czech Republic and Russia are clearly not, but many are hard to classify, John Black *Oxford Dictionary of Economics*, (Oxford, Oxford University Press, 1997)

conditions helps in determining where manufactured goods can best be produced. For example: the British cotton goods industry thrived in towns at the foot of the Pennine Hills because of the natural dampness of the area, it suits the cotton-manufacturing process. The natural, physical and climatic condition is an important determinant of trade. e.g., Zambia has the copper that is required by Britain's vehicle industries, there is very little copper available in British soil. Each motor car contains more than a kilogram of copper, so without the copper there would be no British made vehicles.

International trade there by enables countries to make goods that they otherwise would not be able to make. It thus enables the people to enjoy a wider range of goods and services that would not be available to them if they rely completely on the domestic resources of the economy. Therefore, trade has the capacity to raise the living standards of the people. Thus possessing the resource endowment gives an economy an economic advantage over others who lacks such endowments. Further more when the country specializes in making a product its people become skilled in its production and develop another type of comparatives advantage.[2]

The theory of comparative advantage is one of the very few theories that economist generally agree upon. But in recent years the consensus has begun to crack. Though a major section of world trade is explained by this theory, but historical factors especially the nineteenth century colonialism are powerful influences in deciding the pattern or kind of trade.

2 Lower opportunity costs than other countries. A country has a comparative advantage in producing a good, relative to another country or the rest of the world. If the relative cost o f producing the good, that is, its opportunity cost in terms of other goods forgone, is lower than it is abroad. The law or theory of comparative advantage can be interpreted in either a positive or a normative sense. In its positive sense the law says that countries tend to export goods in which they have a comparative advantage and to import goods in which they have a comparative disadvantage. As real world trade is affected by tariffs, subsidies, and monopoly this is an empirical generalization, not a logical necessity. In its normative sense the theory of comparative advantage says that it is beneficial both for a country and for the world as a whole if trade follows the lines suggested by comparative advantage, John Black, *Oxford Dictionary of Economic*,(Oxford University Press,1997).

The theory states that output and the increase from specialization and exchange will be maximized when each country or region specializes in the production of those goods and services in which its comparative advantage is largest. e.g., country A may be able to produce its own watches, but country B can make it cheaper and of the same quality- it has a comparative advantage over A when it comes to watch making. It may pay country A to buy watches from B and for A to concentrate on making those goods in which it has an advantage over B, and then for A and B to exchange goods. The theory is credited to economist David Ricardo, in his book principles of political economy and taxation.

The theory can be personalized by imagining a carpenter and gardeners who lives next door to each other and who excel in their own job. If they had no contact with each other, the carpenter would have superb furniture in her home but her garden would resemble a overgrown jungle. The gardener, on the other hand would have a beautiful garden but as for her furniture, it would be a case of "pull up a plant pot and sit down". If however the two agree to an exchange- to trade carpentry for gardening skills, then both could have lovely furniture and beautiful gardens. Both can gain from trade and exchange with each other.[3]

One problem with the theory of comparative advantage is that it assumes full employment[4] of resources and that all countries gain from international trade. If unemployment exist then putting resources to work even if there is no comparative advantage may be more important to policy makers than economic

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[3] John Madeley, Trade and the Poor, Intermediate Technology Publications, 1992, pg.6.

[4] A Situation when every worker available for employment has a job. It is very unlikely that this can ever be achieved, even when there is general excess demand in labour market. Some forms of unemployment probably cannot be reduced to zero. These include frictional unemployment, where people leaving jobs in declining sectors of the economy have not yet obtained a job in the expanding sectors. They also include search unemployment, where workers are unemployed while looking for jobs whose type, pay, and working conditions match their expectations. If these expectations are unrealistic it may take some time for them to learn from experience that they are aiming too high. There will also be people whose past or present conduct makes it hard for them to obtain or keep jobs. When economists talk of full employment, they normally mean fairly full employment, in which unemployment has been reduced to the categories mentioned here. Many doubt whether this unemployment level can be sustained if it is below the non-accelerating inflation rate of unemployment. (NAIRU), John Black, Oxford Dictionary of Economic, Oxford University Press, 1997.

theory. And that all countries gain from international trade as the theory proposes has obviously not happened. Some have clearly gained a great deal more than others. Swiss economist Paul Bairoch has estimated that in 1750, GNP per head of people in North and South was about the same, in 1930 it has four times higher in north; 60 years later it is around eight times higher. Under the theory of comparative advantage such imbalances were not supposed to happen.[5] As the theory follows the wages in north would have become so high that manufactures would have all moved their factories to the south to take advantages of cheap labour. At least they would open their new factories or locate their new services in south. But this has not happened to any substantial degree. There are numerous probable reasons. A firm making clothing, set up in Britain exports products to other industrialized countries without barriers. If it set up in Sri Lanka, then it may be able to export only a limited amount because of the international trade restrictions. Businessmen and investors like political stability in this regard they may feel their investment is safer in Britain than in Sri Lanka. In Sri Lanka there may be administrative problems too. It is easier to set up factory in one's own country where he is familiar to the rules rather in third world country where administrative hurdles and unknown factors have to be overcome. Whatever be the reasons the theory of comparative advantage has not led to the flow of venture capital that would equalize wages and living standards between countries. And it has also failed to raise the living standards in the south because of the presence of deeply entrenched historical reasons.

The present pattern of international trade is largely determined by the colonial era of the nineteenth century. The British economist John Stuart Mill said that "Colonies should not be thought of a civilizations or countries at all, but as agricultural establishments whose sole purpose was to supply the larger community to which they belong". The world was divided into a small number of

[5] John Madeley, "Trade and the Poor" , Intermediate Technology Publications, 1992.

countries in the northern hemisphere that industrialized and enjoyed cheap agricultural produce and many countries in the south that provided the cheap produce and purchase the comparatively expensive manufactured goods. The theory of comparative advantage fell down heavily in the twentieth century because it works when the trading nations are roughly equal. Western nations export manufactured goods unlike the countries in the south export chiefly primary products and produce. North-South trade is between a rich block and poor block where the gap between is ever widening.

One of the problems for commodity producing countries is that they face a perfect market for their goods (in the sense that there is general and universal knowledge about them.) For example: the price of coffee beans is known and applied throughout the world. On the other hand companies that make manufactured goods enjoy an 'imperfect' market. Manufactures can claim special features for their goods and fix prices accordingly, thus there is inevitably imperfect knowledge. A manufacturer making radios can claim that this or that gadget is new or different and therefore worthy of a higher price.

Secondly there is often over supply of primary produce so the prices are low. When people become rich in the north they do not increase their consumption of agricultural goods. Hence the demand for these products is hardly expanding where as when the living standards raises the demand for goods like radios, watches etc also rises.

Protectionist barriers imposed by western countries make it difficult for the developing world to branch out into manufactured goods. The west employ not only tariffs, which raises the price of imports but also non tariff barriers. A small number of developing countries have gained economically from international trade. Only the "Gang of four" consisting of Hong Kong, South Korea, Taiwan and Singapore have made tremendous economic progress through international trade. Most of the developing world found it difficult to follow the route of the"Gang of Four". Many Latin American countries have tried but were not able to do with their export led policies. Neither the investment nor the domestic purchasing power exists for all third world countries to industrialize and market manufactured goods in the way of the "Gang of Four".

International trade often led the poor economies to 'Dual economy'[6] and breed inequality within the country. A dual economy comes into being when one modern and relatively well paid and one traditional with low return and poverty coexist. In theory the trickle down[7] hypothesis say the benefit of the modern sector will pull up the traditional sector but in practice this has not happen, the spread effect has been weak.

International trade has helped economic growth in some developing countries but at the cost of agriculture and rural development. It has not helped in broad-based economic and social development. The citizen of an economy which depends greatly on international trade will benefit only when the government has a policy to spread the benefits of the trade.

It appears that the economic impact of trade on most third world economy have widened inequalities within the exporting country. An assessment given by Swedish economist Gunnarmyrdal, "international trades generally tend to breed inequality and do so more strongly when substantial inequalities are already established".[8] The gains from international trade are of little benefit to most of the people in a developing country unless accompanied by appropriate domestic reforms. As Chichilinsky points out that "better terms of trade for the south in their dealings with the north are linked with better distribution of income within the

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6 An economy in which modern industries, mines, or plantation agriculture exist side-by-side with backward sectors, with little interaction between them. This situation may occur in less developed countries (LDCs) with foreign investment in extractive industries using expatriates for their more skilled work. If the rest of the economy consists of subsistence farming and traditional handicrafts, technology transfer from the advanced sector may be minimal, John Black, Oxford Dictionary of Economic, Oxford University Press, 1997.

7 The proposition that economic development benefits the poorest members of a society mainly through the effects of increased national income on the demand d for labour, rather than through explicit measures to assist them, John Black, Oxford Dictionary of Economic, John Black, Oxford University Press, 1997.

8 John Madeley, Trade and The Poor, Intermediate Technology Publications, 1992.

south. The international market is therefore an important factor in shaping domestic distributions within each region".[9] People in the developing countries will gain from trade when the international terms of trade improve and domestic arrangement ensures a fair distribution of income.

HISTORY OF INTERNATIONAL TRADE THEORY

THE THEORY OF ABSOLUTE ADVANTAGE[10]

In the seventeenth and eighteenth centuries, a school of thought gained prominence and popularly known as "mercantilism"[11] according to this school international trade may give rise to an inadequate supply of circulating monetary gold when import will be in excess of export. The economy can not afford to loose its silver and gold as they are mainstays of national wealth and essential to vigorous commerce. So they emphasized on increasing export and less of import. This will prevent the drain of the precious metal.

Imperial rivalries also led to political concerns about the transfer of specie into foreign hand and in part explain colonization efforts in the eighteenth and nineteenth centuries where colonies were seen as a source of raw materials and an outlet for manufactured goods. However, David Hume in 1752 demonstrated that through the price-specie flow mechanism, international trade was likely to maintain equilibrium in the balance of payments. If a country found itself with surplus currency, domestic prices would tend to rise relative to prices of foreign commodities and money would flow out of the country. It a country found itself

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9 Ibid.

10 The use of fewer resources per unit of output than other producers. With only one type of resource, such as hours of work, a producer with lower inputs has an absolute advantage. In a world with many factors of production absolute advantage is often hard to measure. In any case, absolute advantage gives no advice on what to do with resources, which are best employed where their comparative advantage is greatest, John Black, Oxford Dictionary of Economic, Oxford University Press, 1997.

11 A belief in the merits of balance of payments surpluses to increase the money supply and stimulate the economy and advocacy of protectionism to achieve this. Critics claim that in the long run mercantilist policy is self-defeating, as more money increases the price level until any trade surplus vanishes, leaving only real losses form restrictions on trade.

with a shortage of currency, domestic prices would be depressed and would attract foreign currency until the shortage had disappeared.[12]

Adam Smith in the Wealth of Nations (1776) mounted a broader assault on mercantilist theories and argued that the case for gains from specialization in domestic economic activities applied equally to specialization in international trade: "What is prudence in the conduct of every private family can scarcely be folly in that of a great kingdom. If a foreign country can supply us with a commodity cheaper than we can make, better buy it of them with some part of the produce of our own industry".[13]

To have an example, if countries with tropical climates can produce bananas or pineapples more cheaply, than countries with temperate climates than the latter should purchase the product from the former. Conversely if the industrialized economies can produce hydroelectric generators or telephone system more cheaply and of better quality than those that of the countries with a cost advantage in tropical produce, then latter should buy the product from the former. In domestic economy it is established fact that it makes no sense for an individual to try and produce all his or her own food, clothing, medical services, dental services, home construction services and etc. but rather he specializes in producing some goods or services for others and perhaps for some limited subject of his or her own needs, while purchasing requirements to meet remaining need from others who specializes in their productions. It equally follows on Smith's theories that similar specialization would generate mutual gains from trade in international exchanges –the division of labour is limited only by the extent of the market. In Smith's theory, unilateral trade liberalization would be an advantageous policy for a country to pursue, irrespective of the trade policies pursued by others.

[12] Michael J. Trebilcock & Robert House, The Regulation of International Trade, Routledge, London, New York.

[13] Ibid,p.2.

Thus while the mercantilists believe that one nation could gain only at the expense of another nation and advocated strict government control of all economic activity and trade. But Adam Smith (and the other classical economists who followed him) believed that all nations would gain from free trade and strongly advocated the policy of LAISSEZ-FAIRRE[14] (as little government interference with the economic system as possible) free trade would lead to world resources being utilized the most efficient manner and maximization of world welfare. There were to be only a few exceptions to this policy of laissez-faire and free trade. One of these was the protection to industries of national defense.

In view of this belief, it is paradoxical that today most nations impose many restrictions on the free flow of international trade. Trade restrictions are invariably rationalized in terms of national welfare. In reality trade restrictions are advocated by the few industries and their workers who suffer losses of the imports. As such trade restrictions benefit the few at the expense of the many (who pays higher prices for the competing domestic goods).

An illustration of Absolute Advantage

Here is a numerical example of absolute advantage.

Table 1: Absolute Advantage

	U.S.	U.K.
Wheat (Bushels/Man-hour)	6	1
Cloth (yards/man hour)	4	5

14 A policy of complete non-intervention by governments in the economy, leaving all decisions to the market. It there were perfect markets everywhere, with no externalities, and we were indifferent to income distribution, Laissez-faire would be a first best policy. In fact there are numerous market imperfections and many externalities, and there is considerable concern about income distribution. Laissez-faire cannot seriously be defended as first best. There are, however, government failures as well as market failures, and one might attempt to defend Laissez-faire as a second best policy. Most economists nowadays accept a major role for centralized policy in enforcing competition, regulating externalities, and trying to correct some of the income inequalities engendered by free markets, John Black, Oxford Dictionary of Economic, John Black, Oxford University Press, 1997.

The (table 1) shows that one hour of labour time produces six bushels of wheat in the United States but only one in the United Kingdom. On the other hand, one hour of labour times produces five yards of cloth in the United Kingdom but only four, in of labour time. Thus United States has an absolute advantage over the United Kingdom in the production of wheat. The United Kingdom is more efficient or has an absolute advantage over the United States in the production of cloth. With trade United States would specialize in the production of wheat and exchange part of it for British cloth. The opposite holds true for the United Kingdom. If the United States exchanges six bushels of whet (6w) for six yards of British cloth (6c), the United States gain 2c or saves ½ man-hour or 30 minute of labour time (since the United States can only exchange 6w for 4 c domestically). Similarly the 6w that the United Kingdom receives from the United States is equivalent to or would require six man- hour of labour time to produce in United Kingdom. These same six man hours can produce 30 c in the United Kingdom (6 hr times 5 yards of cloth per man –hour). By being able to exchange 6c requiring a little over one hour to produce in the United Kingdom) for 6w with United States the United Kingdom gains 24 c or saves almost five man hours though United Kingdom gains much more than the United States, what is important is the fact that both nations gain from specialization in production and trade.

Absolute advantage only explains a very small fraction of world trade such as the trade between developed and developing countries. But a major portion of world trade is the trade between the developed nations which could not be explained of absolute advantage theory. It remained for David Ricardo, with the law of comparative advantage to explain the basis for and the gains from trade. Absolute advantage is thus a special case of the more general theory of comparative advantage.

THE THEORY OF COMPARATIVE ADVANTAGE

A central question left open by Smith's theory of absolute advantage was: what if a country has no absolute advantage over any of its potential trading partners with respect to any products or services? David Ricardo in his book the principles of political economy published in 1817 provided an answer to this question. His insight came to be known as Theory of Comparative Advantage. He advanced his theory by means of a simple arithmetic example. In his example, England could produce a given quantity of cloth with the labour of 100 men and wine with the labour of 120 men. Portugal in turn produces the same quantity of cloth with the labour of 90 men and same quantity of wine with the labour of 80 men. Thus Portugal enjoyed an absolute advantage over England with respect to the production of both cloth and wine i.e., it could produce a given quantity of cloth or wine with fewer labour inputs than England. Ricardo argued trade was still mutually advantageous assuming fuel employment in both countries when England exported to Portugal the cloth produced by the labour of 100 men in exchange for wine produced by 80 Portuguese she imported wine that would have required the labour of 120 Englishmen to produce. As for Portugal she gained by her 80 men's labour cloth that it would have taken 90 of her labourer to produce. Both countries would be rendered better off through trade.[15]

Take for example a simple domestic instance-suppose a lawyer is more efficient in the provision of legal services than his secretary and also is a more efficient secretary. It takes his secretary twice a long to type a document than the lawyer could do it himself. If it takes the lawyer's secretary two hours to type a document that lawyer does in one hour. The secretary's hourly wage is $20 and lawyer's hourly rate to clients is $200. It is paying for the lawyer to hire her secretary and pay her $40 to type the document in two hours while lawyer himself sells for $200 the hour of his time that would otherwise have been committed to

[15] Michael J. Trebilcock & Robert House, The Regulation of International Trade, Published Routledge, London and New York.

typing the document. In other words both the lawyer and secretary gain from this exchange.

The example at the international context, generalize to the proposition that a country should specialize in producing and exporting goods in which its comparative advantage is greatest or the comparative disadvantage is smallest and should import the goods in which its comparative disadvantage is greatest.

The gains from trade of means of a numerical example

Table 2: Comparative Advantage

	U.S.	U.K.
Wheat (bushels/man hour)	6	1
Cloth (yards/man hour)	4	2

United States (US) would be indifferent to trade if it received only 4 (from United Kingdom (UK) in exchange for 6w since the US can produce exactly 4c domestically by utilizing the resources released in giving up 6w (table 2). And the US would certainly not trade if it receives les than 4c for 6w. Similarly the UK would be indifferent to trade if it had to give 26 for each 1w it received from the United States, and it certainly would not trade if it had to give up more than 2 c for 1w.

Suppose the US could exchange 6w for 6c with the United Kingdom. The US would then gain 2c (or ½ w of labour time) since the US could only exchange 6w for 4c domestically. UK would also gain if the 6w that the UK receives from US would require 6 man hours to produce in the United Kingdom. The UK could instead use these six man-hours to produce 12c and give up only 6c for 6w from the U.S. The UK would gain 6c or save their hours of labour time. Once gain the fact that the UK gains more from trade than the US is not important at this point. What is important is that both nations can gain from trade even if one of them (U.K.) is less efficient than the other in the production of both commodities.

Both the nations gains by exchanging 6w for 6c. Though this is not the only rate of exchange at which mutually beneficial trade can take place. Since the US could exchange 6w for 4c domestically (in the sense that both require 1 men hour to produce), the United States would gain if it could exchange 6w for more than 4c from the UK. On the other hand, in the UK 6w= 12c both require 6 man hour to produce. Anything less than 12 c that the United Kingdom must give up obtaining 6w from the US represents a gain from trade for the UK. To summarize, the US gains to the extent that it can exchange 6w for more than 4c from the UK. The UK gains to the extent that it can give up less than 12 c for 6w from the US. Thus the range for mutually advantageous trade is 4 c <6w <12c

The distance between 12c and 4 c (i.e., 8c) represents the total gains from trade available to or shared of the two nations by trading 6w. For example when 6w are exchanged for 6c the United States gain 2c and the United Kingdom 6c, the total gain then become 8c. The closer the rate of exchange is to 4c=6w (the domestic, or internal, rate in the United States the smaller is the share of the gain going to the United States) and the larger is share of the gain going to the United Kingdom. Similarly the closer the rate of exchange is to 6w=12 (the domestic or internal rate in UK) the greater is the gain of the US relative to that of the U.K. of the US exchanged 6w for 8c with the UK them both nations would gain 4c from a total gain of 8c. If the United States could exchange 6w for10c, it would gain and the UK only 2c. This proves that mutually beneficial trade can take place even if one nation is less efficient than the other in the production of both commodities. The gains from specialization in production and trade have been measured here, in terms of cloth. However, the gains from trade can be measured in terms of wheat also or more realistically in terms of both wheat and cloth. There is one exception to the law of comparative advantage. This happens when the absolute disadvantage that one nation has with respect to another nation is the same in both commodities. For example if one man-hour produced 3w instead of 1 w in the UK and then the UK would be exactly half as productive as the US in both wheat and cloth. The UK (and the US) would then have a comparative advantage in neither commodity and thus no mutually beneficial trade could take place. The reason is that US will trade only if it can exchange 6w for more than 4c. However now, the UK will not be willing to give up more than 4c to obtain 6w from the US because UK can produce either 4w or 4c with two man hours domestically. Under such circumstances, no mutually beneficial trade can take place. This condition modify the statement of the law of comparative advantage to be reed as "even if one nation has an absolute disadvantage with respect to the other nation in the production of both commodities, there is still a basis for the mutually beneficial trade, unless the absolute disadvantage, that one nation has with respect to the other nation is in same proportion for the two commodities.

But this exception is only in theory in reality such coincidence is very rare. So the applicability of the law of comparative advantage is not much affected.

Further natural trade barriers such as transport cost can discourage trade even when some comparative advantage exists. It is an assumption at this point that no such natural or artificial barrier (such as tariffs) exist.

THE FACTOR PROPORTION HYPOTHESIS

While Ricardo's theory of comparative advantage still constitutes the underpinnings of conventional international trade theory his theory has been refined in various ways by subsequent analysis. Ricardo's theory assumed constant cost industry according to which a country would specialize completely in the goods where its comparative advantage was greatest. (Wine in case of Portugal). But reality does not always fit the facts. Portugal produces both wine and some cloth. Ricardo theory was then modified to explain the case by increasing cost industry.

For example there is no guarantee that released resources from cloth-making i.e. the labour inputs would lead to increase in wine production at constant proportions. Especially if the factor proportions in the two activities were different e.g. cloth making in labour intensive while wine making is land intensive. When more than one factor of production is taken into account, it become obvious that combining land and labour at ever increasing levels of output would not necessarily entails similar costs, as the land brought into production at higher levels of output may be less productive and require more intensive use of labour. On the other hand, the opposite phenomenon may sometimes be true, that is the decreasing costs may be associated with increased scale of operations or level of output and may lead to complete international specialization.

Recognition of these consideration left to a reformulation of Ricardo's theory of comparative advantages, and often referred to as the Factor Proportion Hypothesis (or the Heckscher-Ohlin-theorem after two) two Swedish economist who formulated the theorem in 1920's.[16]

According to the factor proportion hypothesis countries will tend to enjoy comparative advantages in producing goods that use their more abundant factors more intensively and each country will end up exporting its abundant factor goods in exchange for the import that use its scarce factors more intensively. While the factor proportions hypothesis seems to explain adequately the patterns of international specialization in many activities, particularly agriculture and natural resources. It tends to provide a less satisfactory explanation of patterns of specialization in manufacturing activities in modern industrialized economies, where it is common to observe countries specializing in different segments of the same or closely analogous produce markets, and simultaneously exporting and importing products in these sectors. Intra-industry trade has accounted for a very high percentage of the total increase in international trade in recent decades. The factor proportion hypothesis assumes that all countries have access to identical technologies of production and that the list of goods which are traded is somehow exogenously given and unaltered by economic activity. However, the pattern of

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[16] Ibid.

specialization and comparative advantage are not exclusively exogenously determined but are dependent on number of endogenous variables such as savings, capital accumulation rates in different countries. The levels and patterns of investment in specialized human capital[17], and the country's commitment to investments in education, research and development and public infrastructure such as transportation and communication systems reflect the patterns of collective investments.

It is also important to note that classical trade theory as described above assumed that physical output from production was (subject to transportation costs) mobile across nations but the factors of production while in most cases mobile within countries were immobile across nations. While this obviously is true for land but it has become dramatically less true of financial capital, technology, human capital and even people in large part because of advances in communications and transport technologies. Thus trade theory has historically focused on international trade in goods and not international mobility of services, capital or people. This focus has been increasingly challenged, as reflected in a rapidly changing trade policy agenda.

THE PRODUCT CYCLE THEORY

Reflecting on the less static, more dynamic and endogenous factor bearing on comparative advantage, Raymond Vernon of the Harvard Business School formulated a product cycle theory of trade in manufactured goods to explain the patterns of international specialization in manufacturing. According to this theory

[17] The present discounted value of the additional productivity, over and above the product of unskilled labour, of people with skills and qualifications. Human capital may be acquired through explicit training, or on the job experience. Like physical capital, it is liable to obsolescence through changes in technology or tastes. Unlike physical capital, it cannot be sold in a society without slavery: this means that it cannot be used as collateral for loans. The training needed to create human capital has to be paid for. Training for firm-specific human capital, which does not improve worker's earning ability outside the firm, can be provided by employers. General or vocational human capital, which can be used by other employers, will increase workers outside earning power, so employers are in general reluctant to provide this type of training. The cost of creating human capital thus mostly falls on individuals or their families, charitable institutions, or the state.

the highly developed and industrialized economies reflecting their superior access to large amounts of financial capital and highly specialized forms of human capital would enjoy a comparative advantage in the research and development intensive stage of product innovation.[18] This stage would focus initially on servicing a small, domestic, and custom- oriented market. The second stage in the product cycle would see products expanded to cater to a mass domestic market. The third stage would see products exported to other countries and perhaps parent companies setting up subsidiaries in other countries to undertake manufacturing there. A latter stage in the product cycle would see the producing technology becoming highly standardized and adopted by producers in other countries, particularly countries with lower labour costs and products is then exported by these countries back to the countries where the innovations has originated. According to Vernon, quasi-rents would be earned by domestic firms early in the product cycle. But these dissipate as the product moves to later stages in the cycle and comparative advantage shifted to other countries.

The product cycle theory of international trade in manufactured goods explains the patterns of specialization observable in many countries in the 1950s and 1960s. In the last two decades it has lost its significance to some extent as an increasing number of countries, like Japan and other newly industrialized countries have acquired many of the same comparative advantages as the older industrialized economies in early stages of the product-cycle through access to large domestic and international sources of capital that have become increasingly mobile and through investments of their own in the human capital, required to achieve a comparative advantage in the early stages of product innovation and manufacture.

It is increasingly recognized that comparative advantages is not exclusively ordained by nature but is in significant part at least the product of deliberate

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[18] Michael J. Trebilcock & Robert House, The Regulation of International Trade, Published Routledge, London and New York.

government policies. This has led to an increased focus in many domestic policies setting on issues of so called industrial policy and at an international level, concerns and accusation over whether foreign government's domestic policies are unfairly shaping or distorting comparative advantage.[19]

DOES TRADE PROMOTE GROWTH

The empirical role of trade on growth has been a subject of controversy. Sachs and Warner (1995) find evidence that thirteen developing countries opened to trade grew at 4.5 per cent annual rate while seventy four developing countries with closed economies grew by a more 0.7 per cent annual rate between 1970 and 1990. Sebastian Edwards (1998). The factor productivity regression, using data for ninety three countries between 1980 and 1990 and nine different indications of trade openness and trade distortions offer robust evidence of a positive impact of trade on growth. Edward stated that lower trade distortions and greater openness result in higher total factor productivity growth. Frankel and Romer (1999) tackle the issue of how to track the causality between trade and income when analyzing the effects of trade on income. They propose the use of countries geographic characteristic as instrumental variables for trade because geographic characteristics are highly correlated with trade but not with income. The effect of trade on income is found to be quantitatively large and robust though of moderately statistical significance. If the trade to GDP ratio increases by 1 per cent point, per capita income increases by 0.5 – 2 percentage points.[20]

An important body of evidence on the impact of trade and growth does not derive from growth regressions but rather from case studies Srinivasan and Bhagwati (1999) review the large body of case studies of country experiences produced at the OECD, the World Bank and the National Bureau of Economic

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19 Ibid.

20 Lewis A. Riverabatiz & Maria Angels Oliva, International Trade Theory Strategies and Evidence, Oxford University Press.

Research (NBER) on the effects of trade liberalization during the 1960s and 1970s. They conclude that this body of evidence, which takes into account numerous country specific factors, offers plausible evidence of a positive impact of trade on growth.

Haberles have pointed out the following benefits that international trades have on economic development.

(i) Trade can lead to the full-utilization of underemployed domestic resources. Through trade a developing nation can move from an inefficient production point inside its production frontiers, with unutilized resources because of insufficient internal demand to a point on its production frontier with trade. Trade thus represents a vent for surplus. This has indeed occurred in many developing nations particularly those in South East Asia and West Africa.

(ii) As trade expands the size of the market, then the benefits of the division of labor and economies scale can be reaped. This has taken place in the production of light manufacturers in small economies such as Taiwan, Hong Kong, Singapore.

(iii) International trade is the vehicles for the transmission of new ideas, new technology and new managerial and other skills.

(iv) Trade stimulates and facilitates the international flow of capital from developed to developing nations.

(v) In several large developing nations such as Brazil and India, the importation of new manufactured products has stimulated domestic demand until efficient domestic production of these goods became feasible.

(vi) International trade is an excellent antimonopoly weapon because it stimulates greater efficiency by domestic producers to meet the challenges of foreign competition. This keeps the cost low and price of the intermediate or semi-finished product used as inputs in other industries. As a whole goods are available at lesser prices.

Critics of international trade can match the impressive list of benefits with an equally impressive list of the allegedly harmful effects of trade. It is true that when most of the gains from trade are taken away by the developed nations there is great deal of dissatisfaction and justification for demands to rectify the situation. But this does not mean trade is actually harmful. In some cases on balance trade have hampered economic development. However, in most cases it is expected to provide invaluable assistance to the development process. This has been confirmed empirically by many researchers. Even China which for security and ideological reasons strove for self-sufficiency, during the 1990s, came to appreciate the potential contribution of trade to its growth and development and is now reaping major benefits from international trade. And so are the former communist countries of Eastern Europe and the republics of the former Soviet Union (central Asian republics) after the disintegration of former Soviet Union.

THE TRADE GROWTH RELATIONSHIP

Generally there is a positive association between export growth and output growth in the LDCS and other developing countries. But this relationship is slightly weak in LDC's as compare to the other developing countries. At any level of export growth a given export growth rates associated with a slightly lower output growth rate in the LDCs than in the other developing countries. The reason why the trade growth relationship in some what weaker in the LDCs than other developing countries is an issue which need investigation. In the 1990's there was a strong nexus between import growth and investment growth in the LDCs. This proves that there lies a strong investment export nexus, increased exports enables increased imports, increased imports again enables increased investment in the domestic economy and increased investment lead to higher economic growth.

The growth in import capacity in the 1990s was slower than export growth. This was because decreased aid inflows and changes in contractual debt service obligations. Increased investment is not very strongly associated with increased economic growth in the LDC's as in other developing countries.

In such a situation international trade cannot work to increase growth rate, in countries where the level and efficiency of investment are not adequate to support sustained economic growth. On the basis of analysis in the Least Developed Countries Report 2000,[21] the major reasons for the breakdown of the investment growth relationship are as follows: (i) constraints on domestic resource mobilization (ii) weakness of the domestic entrepreneurial class (iii) aid ineffectiveness. (iv) Multiple negative effects of external indebtedness.

The basic requirements for ensuring a trade growth relationship in the LDC's are the emergence of a domestic entrepreneurial class oriented towards productive activities, increase and affective international financial and technical assistance, to build production and trade capacities and a durable exit from the debt trap.

LINK BETWEEN INTERNATIONAL TRADE AND POVERTY REDUCTION

International trade is vital for poverty reduction in all developing countries. But this nexus is neither simple nor automatic. In the condition were there is mass poverty as the case with LDC's, poverty reduction needs sustained economic growth that can increase the average household incomes and consumption to a significant extent. To attain sustained poverty reduction an economy can not depend on welfare transfers, though this policy can be used at any moment in time to alleviate instances of the most extreme misery. It calls for the need of efficient development and utilization of productive capacities in a way that the working age population becomes more and more productively employed. International trade can play a powerful role n poverty reduction in the LDC's. Exports and imports play an active role in the process of sustained economic growth, the development

[21] Ibid.

of productive capacities and expansion of employment opportunities and sustainable livelihoods.

In most LDC the primary sector mainly the agriculture sector dominates the employment and production in the economy and the productive capacities are weakly developed. At this point exports enable the acquisition through importation of goods that are necessary for economic growth and poverty reduction, but which are not produced domestically. These include good, manufactured consumer goods, fuel and raw materials, machinery and equipment and means of transport and intermediate inputs and spare parts. Through the export it becomes possible to transform the underutilized natural resources and surplus labour into imports that supports economic growth. But here it is important to mention that the role of growth of export must be sufficiently high so as to meet the growing import requirements or demand. If this does not happen then the sustainability of economic growth will be threatened by the build up of an unsustainable external debt.

International trade is particularly important for poverty reduction in the LDC's because, contrary to the popular belief their "openness" measured by the level of trade integration with the rest of the world is high. In addition to this the LDC's economies are highly import sensitive. Higher the requirement of the imports for the continuation of ongoing economic activities and their development the greater is the import sensitivity of the economy. In LDC import bottlenecks hamper the full utilization of domestic productive capacities. Since the LDC's suffers from shortage of domestic capital good industry and engineering capabilities, the import content of investment process is very high. Lastly for a few LDC's food security is highly dependent on food imports

But this relationship between international trade and poverty reduction is neither automatic nor straight forward. Because of the following factors:

(i) Most LDCs are predominantly natural resource based or agrarian economies when economic growth depends on the development of a range of new capabilities, institutions and services. New agricultural technologies need to be adapted or developed from scratch, in conformity with the countries' agro-climate and soil conditions. Schools, universities, hospital, technical training centers and research and development institutions need to be set up and the existing one is to be improved. Infrastructure like roads needs to be built and extension services need to be built to bring the majority of the agricultural population inside the orbit of the modern economy. Law and order is to be established and strengthened and monopolistic activities needs to be curtailed. All these require investment of all kinds of physical, human, and social and institutional capital and innovation and technological progress as per the necessity of the country. Capital accumulation and technological progress is the engine of growth and international trade is the fuel for the engine. If the fuel dries up, the engine will not run. Thus sustained economic growth requires not only export expansion but also a strong investment export nexus through which imported equipment, raw materials and production inputs is put to good use and lead to continuous improvements in labour productivity in the economy as a whole. This is very difficult in the LDC because of the lack of financial resources available for financing investment and also the week development of domestic entrepreneurial capacities. Many of the central capital accumulation and budgetary processes in the LDCs are highly dependent on international financial assistance and thus the link between international trade and poverty reduction also depends of the efficiency and effectiveness of the delivery of international assistance.

(ii) Secondly the positive role of exports in expanding import capacity in the LDCs needs to be seen in the context of the nature of their BOP constraints.

Almost all LDC economies suffer from president and high trade deficits. In the period 1999-2001 the trade deficit was over 10 per cent of GDP in 25 out of 44 LDCs and over 20 per cent of GDP in 8 of them, only oil exporting countries tend to have trade surplus and in others exports-earning financed only 65 per cent of the LDC's imports in those years.[22] For the LDC's whose major exports are agricultural commodities, export earnings covered a more 54 per cent of total imports. In such cases trade deficits are mainly financed by aid inflows but in recent times the worker's remittances are becoming increasingly important. The link between trade expansion and poverty reduction is threatened if the increase in trade is seen as an opportunity for reducing the aid. If the improvements in export performance is used in debt service obligations and there is decrease in international assistance. This is dangerous as will lead the country on the same spot in spite of the major efforts to finance its own development.

(iii) The third reason for the relationship between international trade and poverty reduction in the LDCs to be complicated is through the national economies of the LDC's are highly integrated with the rest of the world through trade but the lives and livelihood of the majority of the people in LDC are not directly linked with the international economy. In the urban centre, wage employment constitutes a very small faction of total employment in most LDC's. Very little of the informal sector activity is export oriented though some of them are potentially import competing. Added to this for over half of the LDCs food import constitute less than 10 percent of total food consumption.

There is no guarantee that export expansion will lead to a form of economic growth that is inclusive (reduces the incidence of poverty in the economy). Indeed, there is a strong likelihood that "export led growth" will actually turn out to be "enclave led growth". This is a form of economic growth that is concentrated in a

[22] Ibid.

small part of the economy both geographically and sectorally,[23] like the pattern of development in the colonial period in African LDC's. Where there is well connected road and ports supported by ancillary services exited side by side with large underdeveloped hinterlands with majority of the population. Thus is evident from the fact that "dual economy" or lopsided growth is a common characteristic of most of the LDC's.

An inclusive form economic growth need not just the expansion in export but also an economy wide expansion of income earning opportunities, encompassing exports and import competing activities and non tradable and tradable at a rate that exceeds the growth rate of the working age population. The need is not that of simple export expansion but also the promotion of developmental linkages between growing export activities and rest of the economy. For an inclusive process of economic growth it is important to strengthen the development complementarities between agriculture and non-agricultural activities.

MAKING INTERNATIONAL TRADE AND MORE EFFECTIVE MECHANISM OF POVERTY REDUCTION

The policy issue that most of the LDCs are facing at the era of globalization and liberalization is how to promote development and reduce poverty in a very open subsistence-level national economy situated in a very asymmetrically liberalized international economy. In this regard international trade can be made a more effective mechanism of poverty reduction in the LDC. This requires a development approach in three pillars that has to work together coherently and synergistically. The three pillars of this approach are:[24]

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23 Rubers Ricupero, Linking International Trade with Poverty Reduction: Overview, *Foreign Trade Review Quarterly, of IIFT*, vol.XXXIX, no.4, p.63.

24 Ibid.

- Better national development strategies which integrate trade objective as a central component.
- Improvement in the international trade regime including issues which go beyond the scope of the WTO, to reduce international constraints on development in the LDCs.
- Increased and effective international financial and technical assistance for developing production and trade capacities.

Each of these pillars are important for success. Improvement in the international trade regime are a necessary conditions for success since that regime provides the framework for linking trade more effectively with poverty reduction in the LDCs. The increased opportunity for poverty reduction that comes from such improvements to be translated into reality depends on the condition that how this opportunity is grasped at the national level. The fundamental priority is that government formulates and implements national development strategy that integrates trade in such a way that supports poverty reduction. Along with this the development partners of the LDC also need to support these efforts through international financial and technical assistance to build both public and private trade capacities.

These three pillar strategy to make trade a more effective mechanism of poverty reduction in the LDCs need to be embedded within a broad approach of international development policy that includes increased trade opportunities, more effective international financial and technical assistance, deeper debt relief and the promotion of private capital flows and international assistance for technology transfer and acquisition.

At the preset time there is a wide consensus on better national policies, a better international trade regime and better international assistance for trade capacity building. This can make international trade a more effective mechanism of poverty reduction in the LDCs. To be effective the three pillars need to be articulated and implemented in the way that is most appropriate at the present time.

The policy problem for the LDCs is not the level of integration with the world economy but rather the form of integration. The current form of integration is not very conducive to sustained economic growth and poverty reduction. The process of trade liberalization has created a new environment for poverty reduction in the LDCs and new opportunities of economic growth. The issues is how the LDC's supported by their development partners and through a facilitating international trade regime promotes development and poverty reduction in this new environment of globalization and liberalization.

TRADE EXPANSION AND INCLUSIVENESS OF GROWTH PROCESS

Trade poverty relationship is breaking down because export expansion is not associated with an inclusive form of economic growth, that is poverty reducing The limited amount of data makes it difficult to draw general conclusions on the inclusiveness of economic growth.[25] Moreover, indications from the Diagnostic Trade Integration Studies (DTIS) prepared with the context of the integrated framework for trade related technical assistance for the LDCs (IF) provide important evidence of Immiserzing trade tends to occur more often in LDCs with high levels of income inequality. Indeed, there is an urgent need for country case studies on employment and trade in order to have a better indication of what is actually happening. But this report finds that evidences of export led growth of being not inclusive (growth reducing poverty).

The factors that are responsible for achieving an inclusive from of economic growth based on export-expansion are –

First, it is the extent to which export expansion, import substitution and domestic demand expansion each contribute to demand expansion each

[25] Ibid, pp.67-68.

contributes to economic growth. There is evidence that show that the least favourable trade poverty relationship in the LDCs in the 1990s. is found in countries in which export expansion is the most important demand side component of economic growth and in countries in which import substitution is the major demand side component of economic growth. Virtuous trade effects are most likely to occur if there is a balanced pattern of economic growth and in which domestic demand expansion is the major component of economic growth. But export expansion also makes a significant contribution to the overall process.[26]

Second factor is the intensity of domestic resource mobilization effort. It is a striking fact that two-third of cases of an immiserizing trade effect or ambiguous trade effect in the LDC's in the periods 1990-95 and 1995-2000 are related to an increasing domestic resource mobilization effort and falling share of private conscription in GDP. The domestic resources mobilization effort supporting export expansion is positive from the perspective of growth sustainability to extent that it is associated with efficient investment. But it is very difficult for such "belt tightening" to occur in very poor of countries, where the average consumption of the population as a whole is equivalent to just $ 1 a day, without a rising incidence of poverty.[27] If the "belt tightening" associated with export expansion becomes too much then the able growth process may become impossible to be sustained.

The trade off between increased domestic resource mobilization which can help to strengthen export growth, and reduced poverty is a major dilemma in poor countries. The problem is less acute where the average per capita private consumption is not at basic subsistence levels. The trade of between the two desirables goal is loosened if the trade growth relationship is stronger. But If export growth is associated with slow increase in GDP per capita, as it is the many LDC's the trade off is more pronounced. In these circumstances, ensuring that export expansion, increased domestic resource mobilization and poverty reduction

26 Ibid.

27 Ibid.

all occur together depends critically on the availability of external resources to diminish the trade off between resources mobilization and poverty reduction.

TRADE LIBERALIZATION, ECONOMIC GROWTH AND POVERTY REDUCTION STRATEGIES

In this context of Trade Expansion and Inclusiveness of the economic growth process, it is important to note the link between trade liberalization, economic growth and poverty. Since expansion of trade is possible only through liberalization which in return will encourage growth and the economic growth can reduce the extent of poverty.

The widely-accepted view among economists is that, with other things the same, Countries with few restrictions on trade will have faster economic growth than countries that heavily restrict trade, and that absolute poverty will be reduced more quickly with faster economic growth. It follows that countries are encouraged to reduce trade barriers in order to reduce absolute poverty. Trade liberalization is seen as leading to faster economic growth because it reduces distortions in price relativities and allows those activities with a comparative advantage to develop. Poor countries usually have high ratios of labour to land and labour to capital and thus have a comparative advantage in labour-intensive activities. Development of labour-intensive activities in these countries provides income-generating employment for larger numbers of poor people than trade - restricting policies that distort relative prices in favor of capital-intensive activities. But even poor countries with a high ratio of land (or natural resources, more generally) to labour will find that removal of trade barriers that favor capital-intensive industry development will see increased employment of the low -skilled labour. The logic of this argument appears quite straightforward if one understands and accepts the theory of comparative advantage. Why then is there so much resistance to trade liberalization policies—not only from 'anti-globalization' demonstrators but also from within the economics profession? Resistance comes in part from those who lose as the result of the removal of trade barriers. Removal of trade barriers leads to a decline in the value of assets of protected industries and to the loss of jobs in those industries. Therefore, both labour and capital in protected industries will join forces to protest against reductions in trade barriers. But debate over the benefits of trade liberalization for poverty reduction also arises between economists. Differences exist over the impact of trade liberalization on economic growth and over the relationship between economic growth and reductions in poverty. This section reviews these debates and examines whether it is possible to design trade liberalization strategies that will lead to faster economic growth and reductions in absolute poverty. The review shows that trade reform is difficult to implement and sustain and that the trade liberalization strategy adopted should be carefully tailored to the circumstances of the particular country in order to achieve faster growth. Complementary policy reforms and new or improved institutions may often be necessary and the sequencing of these various reforms can be critical. It is contended that a trade liberalization strategy should not be thought of as a policy to reduce absolute poverty. Rather, trade liberalization strategies should be designed so as to achieve trade liberalization in the most effective way and to minimize adjustment costs. The poverty reduction strategy should be separate and should focus on identifying and removing obstacles to the poor participating in economic activities. In this way the impact of trade liberalization on economic growth and the reduction of absolute poverty as the result of growth should both be maximized. Income and food security for labour displaced by the trade liberalization should also be treated as a separate objective and handled with a separate policy instrument. Although, as recognized later, the capacity of poor countries to redistribute income is limited

THE RELATIONSHIP BETWEEN TRADE LIBERALIZATION AND ECONOMIC GROWTH

Broadly there have been three phases in thinking about the relationship between the trade policy regime of a country and its rate of economic growth:

neoclassical, endogenous growth and the institutional approach.[28] In the neoclassical approach, trade patterns among countries are determined by comparative advantage, i.e., where each country maximizes its welfare by concentrating on the activities in which it is most economically efficient. The gains from trade may be static—such as improvements in the allocative efficiency of resources use—or dynamic—such as imported technology or "learning-by-doing" effects. But generally, in the neoclassical theory[29]., trade liberalization does not lead to a long-run increase in the rate of growth, only to an increase in the level of income

The endogenous growth approach[30] found reasons for trade policy to have impacts on both the level of income and the long-run rate of growth of an

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28 **Institutional approach:**

With the resurgence of institutional economics in the 1990s, economists (and aid donors) have turned their attention to the role of institutional factors in examining the impact of changes in levels of tariffs and quotas on economic performance. In the view of New Institutional Economics (NIE), trade reform is institutional reform and the changes in tariffs and quotas typically constitute only a small part of a much more complex process. Trade liberalization is associated with changes in the government's relationship with the private sector and with the rest of the world. Trade liberalization sets new rules and expectations regarding how these policy choices are made and implemented, and establishes new constraints and opportunities for economic policy.

29 **Neoclassical approach**:

The neoclassical approach to the trade-growth nexus invokes general equilibrium models with constant or decreasing returns to scale. Moreover, it is built upon the choices of rational individuals acting solely through markets. Trade patterns among countries are determined by comparative advantage, either in the form of technology differences, as in Ricardian models, or of resource endowments, as in Heckscher-Ohlin models. The neoclassical models of international trade theory in general predict that a country will have static gains from lowering its trade barriers .Perhaps one of the most important static gains from trade liberalization predicted by neoclassical models is the increase in allocative efficiency. Since trade policy has an important impact on the transmission of international price signals, lowering trade barriers will lead to a reallocation of resources to the sectors with comparative advantage. As a result, resources are used more efficiently and the welfare of the country as a whole will rise .Another gain from trade liberalization predicted in some neoclassical studies linking trade and productivity is that lowering trade barriers can create a so-called X-efficiency gain by having a positive impact on the efforts of workers and managers in the economy. Increased foreign competition due to lower barriers has an invigorating effect similar to that of a "cold shower" and workers/managers have to raise their efforts to survive the fiercer foreign competition. Yet the gains from trade liberalization are—by nature of the neoclassical models—static, and trade policy like other government policies has only level effects, not growth effects—a well-known prediction of neoclassical growth models as in Solow (1956) and Swan (1956).

30 **Endogenous growth approach:**

The dynamic gains of trade liberalization are closely linked to writings on endogenous growth ("new growth") theory that have proliferated since the mid-1980s. Much has been made of the endogenous growth theory, however, in many ways it differs only slightly from the neoclassical model. Certain economy through scale, allocation, spillover, and redundancy effects. Scale effects are assumed to be derived from the closer integration of the country with the world market, while allocative effects arise from the resource reallocation leading to the accumulation of factors of production such as human or physical capital or R&D. For developing countries, protection that denies access to imported capital goods embodying improved technology is thought to be a particularly growth-inhibiting factor. The spillover effect is a related effect with trade leading to the diffusion of new knowledge

IMPACT OF GROWTH ON POVERTY

The relationship between growth, income inequality, and poverty has been one of the central points of discussion in the development literature. There has been tremendous emphasis placed on the probable trade-offs between growth and income inequality. The relationship between growth and income inequality was proposed to resemble an inverted U curve; that is, income inequality increases in the initial phases of development, then declines as growth continues. This view was derived from the path-breaking work of Kuznets (1955) who investigated a time series of inequality indicators for England, Germany, and the United States. There are some mechanisms that may generate the famous Kuznets curve. One widely cited mechanism is the transfer of labour from a sector with low productivity and low inequality to another sector with higher productivity and

features are common to all growth models. First, they incorporate a produced "accumulable" factor, which is a durable input whose stock increases over time—physical capital, human capital, or technology. Second, if an increase in the productivity of the inputs producing the accumulable factor occurs at some point, an increase will occur in the rate of accumulation and the growth of output in subsequent periods. A key difference between the neoclassical and endogenous growth models is how long this increased growth lasts. In neoclassical theory, the increase in the growth rate eventually converges to zero, whereas in the endogenous growth theory the increase can be permanent. The source of this difference is the assumptions about the income share of the accumulable factor. If this share is low, as in the neoclassical model, any increase in, say, capital, in one period does not yield a large increase in production of capital, thus dampening the accumulation process, causing it to converge. If the share is high, as in the endogenous growth models, any increase in capital inputs will yield a larger increase in production of new capital, causing the accumulation process to last longer, possibly indefinitely, in which case permanent growth effects are possible higher inequality as in the model proposed by the seminal work of Lewis (1954). The result would hold if the inequality between the sectors was substantially greater than the inequality within them. Aghion and Bolton (1997) propose another mechanism with trickle -down effects of capital accumulation. In their work, the increased wealth of the rich implies more funds available for investment by the poor, and the accumulated wealth of the rich trickles down to the poor through borrowing and lending in the capital market. In the presence of imperfect capital markets, their model can generate a Kuznets curve. The Kuznets hypothesis has been exposed to a large number of tests over the past four decades. Recent studies using data from developing countries generally refute the inverted-U relationship between the level of income and level of income inequality. Deininger and Squire (1998) provide the most comprehensive test so far of this hypothesis with a data set of relatively good quality and comparable data for several points of time for individual countries. They conclude that "our data provide little support for an inverted-U relationship between levels of income and inequality, when tested on a country-by-country basis, with no support for the existence of a Kuznets curve in about 90 per cent of the countries investigated." (Deininger and Squire 1998:573).[31] In another empirical study, Ravallion and Chen (1997) conclude that growth seems to reduce inequality in the transitional economies of Eastern Europe and Central Asia. However, their work and other empirical studies show that the pattern of income distribution in developing countries has been fairly stable over a long period of time (Dollar and Kraay, 2001a and Deininger and Squire, 1998). Still, the empirical evidence about the relationship between income inequality and economic performance is fairly mixed and the outcome far from being settled. While Benabou (1996) reports that the vast majority of the empirical studies up to 1995 on this relationship reach the

[31] Ron Duncan and Doan, Trade Liberalization, Economic Growth and Poverty Reduction Strategies, Quang National Centre for Development Studies .The Australian National University. Available at: www. ausaid. gov.au/research/pdf/trade_and_poverty.pdf -

conclusion that there is a negative correlation between inequality and growth, Forbes (2000) employs a new and better quality data set and finds a positive and significant relationship between inequality and growth. However, the difference in empirical studies can be in part attributed to econometric differences, in the econometric approach and the choice of variables. A clear distinction should be made, however, between income inequality (and relative poverty) and absolute poverty. Available data provide overwhelming evidence that economic growth contributes to reductions in absolute poverty, not only in empirical studies investigating individual countries but also in cross-country studies. Ravallion and Chen (1997) claim that there is a statistically significant negative relationship between absolute poverty and growth. In a study of 92 countries spanning four decades, Dollar and Kraay (2001b) find that the average incomes of the poorest one-fifth of society rise in proportion to average incomes. They were unable to isolate any factors that account for this empirical regularity, illustrating how little is known about the relationship. Unlike the trade-growth nexus, however, the relationship between growth and absolute poverty reduction does not generate significant debate among economists and policy makers, although there is some dispute about the rate of economic growth at which absolute poverty begins to fall. It should be noted that it is possible that growth can be biased against the poor so that with a sufficiently large increase in income inequality, the outcome can be a rise in absolute poverty. This behavior was observed in the Philippines over the period between 1988 and 1991 (Ahuja *et al.* 1997:47). Import-substitution trade policies that favor capital-intensive industries rather than labour-intensive industries and forms of exploitation of natural resources that generate benefits concentrated in a small part of the population could have such an impact.[32]

[32] Ron Duncan and Doan Quang Trade Liberalization, Economic Growth and Poverty Reduction Strategies National Centre for Development Studies The Australian National University. Available at: www. ausaid. gov.au/research/pdf/trade_and_poverty.pdf -

CHAPTER – 2

PROBLEMS AND ISSUES

CHAPTER 2

PROBLEMS AND ISSUES

INTRODUCTION

This chapter aims to describe the problems that the Central Asian state are facing in their path of economic liberalization, since they are in transition phase the problems are very complex and are faced with critical issues. The problem varies from social political and economic in nature. The discussion here is limited to economic problem in the context of foreign trade related issues. In this period of Globalization when the Central Asian state are trying to Liberalize they are confronted with certain obstacle and dilemmas like the debate between regionalism and multilateralism .The first section deals with the issue of economic integration and trade diversification challenges , prospect with CIS and the debate between regional economic integration and multilateralism. Second section desribes the trade barriers and the obstacles that is hindering the growth of foreign trade. The description has been confined to the aspects that are more important and critical at present stage.

As Kyrgyz Republic is only economy of Central Asia that is member of WTO, hence the discussion in case of Kyrgyz republic is in the light of membership. This chapter also intends to analyze the major problems and issues that Central Asian economies are facing in this period of liberalization and globalization.

The Central Asian states comprising of Kazakhstan, Kyrgyzstan, Tajikistan, Turkmenistan and Uzbekistan are rich in natural resources. This region is abundant with minerals, especially hydrocarbon resource. These states are newly independent and were part of Soviet Union. They were not only politically integrated with USSR but were also economically integrated with the political separation countries need to separate on economic lines. They are organizing their economies on their own. They have established their own central banks, currencies and other economic and financial institution. This also hold true in the field of trade also. The Central Asian countries are conducting their foreign trade with increasing openness and confidence. These countries are widening the space of cooperation by collaborating with multinationals and others to enhance the pace and progress of their economic development. This policy have resulted in the arrival of host of multinationals in energy and other sectors of these economies and Central Asia has become one of the focal point of global economic interests. The Central Asian states have unlimited growth potential. Once the natural resources especially hydrocarbon resources from these Central Asian states reach the international market, the potential of growth in these economies in very high. The growing markets in these Central Asian countries are reported to have the potential of becoming one like the gulf countries. Therefore the Central Asian states that are going through the period of economic transition have very bright future prospects owing to the abundance of its natural resources. In this period of transition the centralizing states faces the dilemma of regionalism vs. multilateralism, this has been the major issue for all the Central Asian states.

ECONOMIC INTEGRATION REGIONALISM AND MULTILATERALISM

The literature on regionalism versus multilateralism is growing as economist and political scientists grapple with the question of whether regional integration arrangements are good or bad for the multilateral system. Are regional integration arrangements "building blocks or stumbling blocks", in Jagadish Bhagwati's phrase, or steppiong stones toward multilaterlism? As economist worry about the ability of the WTO to maintain the GATT's unsteady yet distinct momentum toward liberalisation and as they contemplate the emergence of world-scale regional integration arrangements (the EU, NAFTA, FTAA, APEC and possibly, TAFTA), the question has been more pressing.[1]

As the concept goes that regional trade agreement right act as building blocs for multilateral trade liberalisation comes originally out of game theory 'The pace by which any government can bring their communities along with trade liberalization is a critical factor in political economy. Certainly multilateral liberalization is the first best option. But it may be easier to negotiate with a set of countries rather smaller in number than the universe of all countries or practically speaking all contracting parties to the GATT[2] or today the 130 plus WTO[3] members. In most cases such a process takes place among contiguous countries whose cost structures are very similar as it implies a lesser degree of economic adjustment for bilateral liberalisation. On the other hand sector specific lobbies are dangerous as, if regionalism is permitted because they tend to stop blocs from moving all the way to global free trade. In the presence of lobbies, trade division is good politics even if it is bad economies Regionalism's direct effect it has on multilateralism is important but possibly more so is the indirect affect it has by changing the way in which group of countries interact and respond to shocks in the world economy. Regionalism, allows stronger internalization of the gains from trade and liberalization is likely to facilitate freer trade when it is highly restricted. The possibility of regionalism probably increases the risks of catastrophe in the

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1 L. Alam Winters, Regionalism versus Multilateralism, http://econ.worldbank.org/files

2 General Agreement on Tariffs and Trade on Agency of the United Nations (US) based in Geneva, founded in 1948 to promote international trade by 1995 it had over 100 members, including most leading trading countries. GATT successfully concluded several rounds of multilateral negotiations to reduce world tariffs, but was unable to prevent the spread of non-tariff barriers to trade such as voluntary export restraints (VERS). The latest round of GATT negotiations, the Uruguay Round finished in 1994, this included measures affecting trade in agricultural products and services and intellectual property rights of all of which had been omitted from earlier rounds. it also led to the replacement of GATT of world trade organization (WTO).

3 An International body to supervise and encourage international trade. An international trade organization was proposed following the Breton Wood Conference in 1994 but was never set up. The GATT was started instead. GATT organized the Uruguay round trade talks which concluded in 1994 of setting up the WTO to take over its functions in encouraging multilateral trade in goods and services.

trading system. The insurance incentives for joining regional arrangements, and the existence of "shiftable externalities", both leads to this conclusion. And the view that regionalism is a means to bring trade partners to the multilateral negotiating table are because it is coercive. Using regionalism for this purpose could have been an effective strategy but it is also very risky.

There are differing views about the benefits and costs of regional trading agreements Economist may agree that multilateral agreements are the preferred instrument for liberalizing international trade. As such an agreement ensures a non-discriminatory approach which provides political and economic benefits for all. The current political environment as demonstrated by the failure of the Cancun ministerial is not particularly favourable for multilateral trade negotiations. There are numerous important and unresolved issues in the WTO negotiation. 2004 is a critical year for the WTO and agreement must be reached soon on the modalities of these negotiations or they are likely to drift on indefinitely. It is against this background that more and more countries have turned their attention to regional trading arrangements. Countries are taking that route because such agreements are often a more practical and feasible way to liberalize trade. Regional trading agreements can bring faster results than the multilateral process. They may enable the parties to make commitments that are more meaningful and more trade liberalizing than a multilateral undertaking.[4] They even address issues that are not even on the multilateral agenda. Regional trading arrangement can be valuable in dealing with tough issues that often cause deadlocks on the multilateral front in areas such as services and government procurement. At the same time, regional trading agreements have negative effects as well. It diverts trade away from lower cost producers outside the bloc. They also can undermine the multilateral system because of their inherently discriminatory nature. Each regional trading arrangement establishes its own rules of origin, and that can have important

[4] Regionalism versus multilaterally A statement by Timothy E. Deal Senior Vice President http://www.USCIb.org/index.asp

adverse effects. Preferential rules of origin can stifle innovation; impede the creation of networks and joint manufacturing and unduly third country sourcing leading to trade diversion. This proliferation of divergent rules of origin increases the transaction cost for business and it slows processing times at borders as the OCED[5] pointed out: "It is not uncommon for a single country to have to apply different sets of rules when determining how to classify the origin of goods being traded, depending on the RTAs to which it belongs. This complicates both the production and sourcing decisions of companies established or considering establishment in that country".[6]

The slow paces of multilateral negotiations have given a greater impetus to bilateral and regional trade negotiation. But the very success of those negotiations can make liberalization on a multilateral scale more difficult as government devote greater time and attention to deals that can be consummated quickly. They further detract from multilateral efforts by stretching already scarce negotiating resources, especially in developing countries. Unless government takes care to balance their regional aspirations with global commitments, the end result could be competitive discrimination. Regional trading arrangement can complement but not substitute for, coherent multilateral rules and progressive multilateral liberalization.

Further, since the process of trade liberalization requires political sustenance from whatever corner it can acquire, Political sustenance, regional trade agreements usually have an overt political character from which they gather support. For serious policy makers trade diversion costs are genuine concern, who understand that trade policy is not a diplomatic game. If preferential agreements are formed, driving down to zero tariffs without import licensing system under whatever guise. It would impose considerable foreign exchange cost on the

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5 Organization for Economic Cooperation and Development, An international organization set up to assist member states to develop economic and social policies to promote sustained economic growth with financial stability. OECD members have been mainly fuel-market industrialized countries.

6 Regionalism versus multilateralism a statement by Timothy E. Deal Senior Vice President http://www.USCIb.org/index.asp

domestic economy. In extreme this could even lead to the phenomenon of perverse resource allocation. It is to note that this issue has an implied quantitative matter that is there may be trade diversion cost associated with regional trade agreements. But the real issues are (a) how much? And (b) for how long can the economy bear the implied foreign exchange cost but by entering into a regional trading arrangement with a country or countries that may not be the most efficient source of import in many areas.

REGIONAL ECONOMIC COOPERATION AND CIS

Ever since the Central Asian states became independent in December 1991, the questions of economic integration either among themselves or within the commonwealth of independent states have become an important issue. Since the regions have common problems, posses similar culture, have greater contact with each other, these common problems can be solved more effectively by pooling of resources rather than unilateral action. Blocs with cultural similarities are more apt to form blocs with each other.

All the states of the of the former soviet union face daunting problems like ethnic turmoil (real and potential), the problems facing economic transition, state building from scratch, environmental and public health etc.[7] Along with this the Central Asian states share a variety of problems like environmental degradation in the Caspian and the Aral Sea, water resource management, security concerns, transport and economic restructuring.

It is to be analysed that whether the common problems are strong enough to produce a well developed cooperative effort, or is the interdependence among the Central Asian states will help them to form a strong economic entity or it is only a potential possibility than being getting converted to reality. As the Central Asian States live in the shadow of Russia, the fear of Russian imperialist motive is a

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[7] Rama Sampath Kumar, Economic Integration –the Central Asian Dilemma. Prof. Shams-ud-din edited "*Nationalism in Russia and Central Asian Republics ,unfinished democratic revolutions*" (New Delhi Lancer Book Publication 1999),p.169.

good reason for these states to work together to counterbalance the common foe, by means of pushing together for a stronger regional structure.

There is another choice as to see whether the CIS as an economic unit is a better alternative to the Central Asian States forming a regional bloc. The integration with CIS also offer them bright prospect of economic development.

Since 1991 the Central Asian states have met on several occasions to promote cooperation and creation of multilateral institution both within and outside the CIS structure. But the progresses in this direction have been limited and these states continue to look towards Russia. In the first place these states were not prepared for the independence that was thrust on them. And after the Slavic states formed the CIS the leaders of Central Asian States met in Ashgabat to check out their future plan of action. They recognized that they should try and work in agreement since they all are poorly prepared economically to face the problems of transition and they have similar initial conditions and similar problems.

As they were looking for new potential sources of financial and technological assistance with the collapse of the USSR's political centre, necessitated that the CAS reassess their geopolitical situation. After lot of discussion it was decided that a Central Asian alternative is not preferable to the CIS. This decision was based on the fact that links with Russia will have preference and will be put above any blue print for a greater Central Asia, as the CIS bound to become a tool in the hands of Russia to influence and put pressure on the Central Asian states. At the same time the Central Asian states were very enthusiastic for a new economic confederation on the lines of the European community.

Since their independence various meetings were held with regard to economic integration/cooperation. In 1992 the five states held regular negotiations and agreed in principle to the eventual establishment of a Central Asian Common Market. In April 1992 at Bishkek agreements were signed to coordinate economic reforms and price policies and create multilateral institutions for monetary and investment co-operation. In early 1993 more concrete discussion were held for creating a Central Asian economic co-operation area, since the promise of the CIS on the economic route were not showing any sings of bearing fruits.[8] This made the case or creating a common economic space and inter-governmental council in 1994, among Kazakhstan, Uzbekistan and a more ambitions proposals for a European Union style common market by the year 2000. There were also talks for trilateral military cooperation. The urge for strong economic cooperation among the Central Asian states led in Feb 1995, soon after the CIS summit in Almaty, to an agreement to form a Central Asian Economic Union (CAEU) among Kazakhstan, Uzbekistan and Kyrgyzstan. This was done on the initiative of Islam Karimov who was interested in creating a Central Asian states entity called "Turkestan" and although both Kazakhsatan and Kyrgyzstan saw the advantages a regional economic grouping, there were apprehensive about the way it would function because of Uzbekistan's dominance. In this way, the Central Asian states resemble the Arab League with a constant desire for a union and their equally consistent inability to implement it. The Central Asian states are finding it very difficult to put cooperative economic union into practice because they have long been used to dealing with Moscow and are also unable to directly deal effectively on a bilateral basis. But they have come to realize that such contacts are desirable for the future and regional cooperation and it does seem to have hopes of greater success in the near future. In September 1995, the members of the Central Asian Economic Union reported satisfactory progress on the path of regional integration. They also invited Turkmenistan and Tajikistan and Azerbaijan to join them. Turkmenistan which was against this for a long time agreed to join this in an effort to promote regional economic transition.[9]

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8 Ibid p.171.

9 Ibid p.172.

The economic structures of these economies are such that they work as impediments to regional economic cooperative effort. It is claimed that since the Central Asian states are highly diversified and complementary and thus it is conducive to trade greater economic co-ordination.

This area is rich in natural resources as it possesses vast amounts of fossil fuels and industrial minerals. Inspite of its abundance of natural resources this region is unable to become a viable and cohesive economic unit. It is because they lack the diversification and the network of economic ties, the infrastructure for export specialization as it is in the Middle East or huge investments from one of the partners as in the case of NAFTA.[10] They has always been depending on Russia for many essential good, the infrastructure (railways, pipelines) that in present ensures the link with Russia for the foreseeable future and holds more prospects than any Central Asian Common market.

Central Asia has inherited a deficient and unbalanced and underdeveloped economy from soviet regime, as the main objective of soviet regime was one of economic extraction, which has created a long term economic and technological dependency. For example the economic importance of Central Asia was the source of essential raw materials for Russia. In the Soviet era Central Asia was the supplier of cheap raw materials and supplier of essential goods like fuel and foodstuffs. Central Asia was excluded from textile manufacturing and rendered dependent on Russia even for cloth manufactured from its own cotton. With more than 70% of Central Asia's best arable lands under cotton dependency on Russia for staple food grew more and more. This "super specialization" in cotton production had degenerated Uzbekistan into a dictatorship of a single crop that drove all other needs of the region from the minds of the leaders. Turkmenistan imports 69% of its food stuffs from Russia. Russia is able to convert this economic

[10] An agreement released in 1993 between Canada Mexico and the United States making these countries into a free-trade area.

dependency into political leverage. The same is true or Kazakhstan[11] for example Central Asia's energy resources, the Central Asian states are unable to convert this tremendous energy supplies to economic power. It is only after the break up of the soviet union that the importance of the southern fringe of the former soviet union have increased dramatically as new explorations have revealed that this area has the potential to become an increasingly important source of energy for the industrialized world and has led to prediction that the Caspian may well be the Persian Gulf of the 21st century. Initially the Central Asian states were confident that the oil and gas resources would be an easy escape from domination of Russia. Since their economies are still linked to the former Soviet Union it is the functioning of the CIS rather than the creation of a new Turkestan seems more acceptable to the Central Asian leaders. The various attempts made towards regional economic cooperation that could lead to integration did not seem to go right and infact attempts towards this was no where successful. Take for example the creation of a new ruble zone. Both the Kazakh and Uzbek President took the initiative for a common Central Asian currency, along with a customs union to regulate the flow of goods from Russia at the discounted prices to which the Central Asian states had grown accustomed. But they could not stop Moscow's continued control of the Rouble and the latter continued to print notes to counter the increase in prices. This resulted in hyper-inflation in the Central Asian states leading to trade deficits and further economic collapse. Inspite of the desperate attempts of the Kazakhstan and Uzbekistan to stay in the rouble zone they had to finally broke the monetary ties with Russia by introducing her own currency the "Some" in May 1993, President Akayev's action was unilateral and in defiance with his commitment to regional economic cooperation. Though the Central Asian states put a unified position against Moscow by introducing a common currency, it should have strengthened their intra-regional economic ties; surprisingly they tried

[11] Ibid p.173.

to hold on to the ruble. The national currencies are not immune to the hyper inflation. They introduced their own local currencies but they were still unprepared and central Asian State were immediately faced with surging inflation, US$ black marketing and acute of goods, worsening honeys and greater dependency on barter trade. Kazakhstan was perhaps the only central Asian States that was able to handle its currency crisis marginally better. These developments in economic history of the Central Asian States prepare strongly the case much against regional economic integration.

Although the CIS has not been effective in promoting economic growth or co-operation among the central Asian states yet they had join it. The reason was the fear of being dominated by Uzbekistan. Among the central Asian states there is no clear dominant power like Germany in the European Union, yet Uzbekistan is positioned to become the anchor state in this region. It has the largest population of the five states and is the predominant Diaspora in central Asia after Russia. Its location is strategic and is the only state that can boast of an usable army. So it can use the economic integration among the weaker states to counter intra bloc threats. The effort to push forward the European monetary unit is an effort by smaller states to limit German Power. But because such economic integration between the Central Asian States does not seem feasible the other states fearing domination by Uzbekistan feel the CIS a better alternative to a "Greater Turkestan".[12] Besides, they all have realized and accept that fact that they cannot easily move out of Russia's grip because of its prolonged dependence and the kind of economy they have inherited from soviet regime. So they feel it is better not to do anything to invite Russia's wrath that will end upon economic pressures. Though the former Soviet Union had collapsed the economic chains that bond them together cannot be that easily broken. So they felt that the CIS was a better alternative for the time

[12] ibid p 178.

being. Each state has its own special reasons for the ties with the CIS and for accepting Russia as the unifying factor.

Turkmenistan initially preferred central control to independence but soon after joining the CIS, displayed opposition to any centralized structure with the CIS. As a token of his protest president-Niazov shunned the body in early 1993 when it appeared that Russia and Kazakhstan were trying to build the CIS into a possible confederation of former Soviet republic. It preferred bilateral agreement with the other CIS and Central Asian states. In May 1993 Turkmenistan refused to sign a declaration of intent to establish an economic union and this was out of the concern that Turkmenistan would be forced to sell natural gas to CIS countries at reduced prices. It played an anti-Russian card, discriminating against the 400,000 ethnic Russians out of a total population of 4.5 million. Moscow retaliated by stopping the food supplies and clamped down on bilateral trade. Turkmenistan relied on Russia for access to western market to sell its gas. Turkmenistan also realized that one of the major outstanding problems was the poor payment record of CIS states for Turkmenistan gas. Russia's help was required to receive payments for gas from the newly formed states of the Former Soviet Union. So Niazov realized that he has to stay close to Moscow and acknowledged Russia's strategic interests in Central Asia. Practical measures to build back the relation took the form of dual citizenship, troop deployment and increased participation by Turkmenistan in the CIS. In terms of security too Turkmenistan relies on Russia to protect its borers with Iran and Afghanistan and also the overpowering Uzbekistan. Uzbekistan is the dominant regional power and not keen on its ties with Russia. But Uzbek-Russia relations grew stronger as a result of the conflict in Tajikistan and Afghanistan. Both countries have a vested interest in the regional stability. Uzbekistan cotton requires the CIS market. For this the Russian help is required. Further the airline industry in Uzbekistan is almost entirely handed by Russians.

It was only Kazakhstan that was keen on closer ties with CIS because of its ties with Russia. Russia was and it remains Kazakhstan's major trading partner. Russia controls access to its export routes of oil and gas. Therefore, it cannot afford to alienate as the impact of it's would be particularly damaging for the Kazakh economy.

Kyrgyzstan also perceives Uzbekistan as the strongest power in the region. After its independence there was social unrest between the country's ethnic Kyrgyz and Uzbek population. It is to counter the threat from Uzbekistan; Kygyzstan sought ties and integration with the CIS, relying on Russia to hold the Uzbek in check. President Akayev's support for the CIS endeared him to Moscow. In 1996 $132 million of Kyrgyzstan debt to the Russian federation was paid off in equity stakes in 39 industrial firms.

Tajikistan is the only state that is 100% dependent on Russian chiefly due to military support it receives. The close relationship has irked the Uzbek president and in Tashkent. The Tajik president is often referred to as "Russia's Man." Some Russian is not happy about being drawn into Tajik conflict viewing it from the Afghanistan and Chechnya experience. But the Russian military presence in Tajikistan has certainly contributed towards increased Russian influence in Central Asia.

OTHER ALLIANCES

This does not imply that the central Asian states are turning away from the rest of the world. They are trying to broaden their economic ties with the west and neighbours such as Turkey, Iran and China. But yet, the success achieve is not of much significance. The competition for capital and aid brings fresh rivalry among the Central Asian states as economic gains weigh more than geography or fraternal ties. Further international ties may put various states in various directions coming in the way of regional cooperation.

The Economic Cooperation Organization (ECO) remained in hibernation for long, at the emergence of the five Central Asian States realized the drastic changes in the geo-political codes of the regional power. Turkey, Iran and Pakistan felt that with the Central Asian States they would be able to emerge as a strong economic block. Based on the fact that they represent Muslim economic unity it is certainly a good instrument to deploy certain regional assets but it has not proved more than a forum to discuss possibilities of regional cooperation.

THE COMMODITY COMPOSITION OF EXPORTS AND THE DIVERSIFICATION CHALLENGE

The central Asian economies have a concentrated commodity composition of export as presented in the (Table 3) below[13]. Kazakhstan is a major oil exporter and it has a large reserve that is yet to be exploited. The country's current exports include a variety of minerals and other regional products. Over half of Uzbekistan's export earnings come from cotton and gold.[14]

These commodities will remain important and valuable export earner in the foreseeable future[15] and the keys to their development are well-known, at least in principle.[16]

For oil exporter, pipelines, agreements are the most important agreement owing to the dominance of pipelines as transport technology. The Caspian oil exporter will realize it full potential in the coming years as will construction of

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13 Richard Pomfret, key trade and investment Challenges for the economies in the Caucasus and central Asia (Richard Pompret@adellaide.edu.au).

14 Among the other countries, Tajikistan is heavily dependent on a single complex whose aluminum must be shipped by rail via Uzbekistan and other transit countries; the Kyrgyz Republic depends on the output of a goldmine whose life span is limited. For all of the central Asian countries cotton is significant export, although for Kazakhstan it is important only for the southern part of the country.

15 As emphasis by Federation Bonaglia and Kiichiro Fukasaku ("Export Diversification in low-income countries: An international challenge after Doha", OECD Development Centre Technical Papers No. 209, Paris, June 2003, pp. 12-13). "Countries rich in natural resources should not ignore their wealth but rather use it to build new areas of competitive advantage. Resource based sector can be a source of knowledge and technological advancement, as exemplified of the historical experience, of both OECD and non OECD economies").

16 Key trade and investment challenges for the economies in the Caucasus and central Asia by Richard Pompret (Richard Pomfreet @ adelaide.edu.are).

value of non primary sector is still very small. An obstacle to FDI in all of the Central Asian countries is the domestic economic environment.[20]

This raise questions as to how to encourage export diversification. The diversification of export and attracting FDI are interrelated. Because of the fact that most attractive FDI is possible in export oriented activities as this cater to wider markets other than the domestic economies.

Table 3: Major Export

	Major export (sharing of total export in parenthesis)	Share of top there interim in total export
Kazakhstan	Crude petroleum (37) Refined copper (7) Ferro alloys (4)	48
Kyrgyz Republic	Gold (35), Cotton (12) Tobacco (11)	58
Tajikistan	Aluminum (47) Cotton (24) Cotton Fabrics (5)	76
Uzbekistan	Cotton (47) Gold (8)	56

Source: Background paper – based on data from UN, Comrade Database 2003.

Table 4: Inward Foreign Direct Investment (Stock in million US dollars 2002)

Kazakhstan	15354
Kyrgyz Republic	415
Tajikistan	162
Turkmenistan	1163
Uzbekistan	1,332

Source: UNCTAD, World Investment Report 2003, Annex B, p. 259.

20 Even where the policy environment is not a major problem (the Kyrgyz republic is the most plausible example) 'the market economy still does not junction well due to their markets and poorly developed institutions.

TRADE BARRIERS

Trade barriers elude fixed definitions, it can be broadly defined as government laws, regulations, policies, or practices that either protect domestic product from foreign competition or artificially stimulate exports of particular domestic products through the method of export subsidies. The government imposed measures and policies that restrict prevent or impede the international exchange of goods and services and included in trade barriers for example the import policy, standard testing labeling and certification, government procurement export subsidies, service barriers, investment barriers etc.

KAZAKHSTAN

Stretching from the Caspian sea to China and from Siberia to spectacular Tianshan mountains, Kazakhstan is a landlocked country the size of western Europe with a population of 15.2 million rich in minerals, with oil and gas reserves estimated to rival those in the North sea, it aims to be one of the world's top ten oil exporters within the next decade. Since its independence from the former Soviet Union in December 1991, Kazakhstan has made considerable progress with economic and structural reforms, achieving macroeconomic stabilization. However, the process is still ongoing with rapid changes occurring in all sectors with the emphasis on reform and openness and integration into international trade and commerce Kazakhstan offers ample opportunities for foreign investment. Most investment in Kazakhstan to date has been in the oil and gas sectors. Kazakhstan external position is improving from the time of its independence due to the growing oil export prices. The petroleum sector accounts for almost one third of gross domestic product (GDP) and well over one-half of all export earnings.

Customs Barrier

Kazakhstan's new customs code became effective from May 1, 2003, superseding the law of 1995. There are positive changes in the code, such as provision intended to provide WTO-compliant customs valuation methodologies. However, as of January 2004, importers continued to report that customs officials were failing to comply with these methodologies.[21] In addition the key provisions for such practices as voluntary disclosure were not included in the code. In September 2004, the customs control Agency was subordinated to the ministry of finance. The customs control Agency continues to discuss the automation of customs procedures but little progress has been made. Since October 2002, Kazakhstan maintained a 'customs audit" procedures administered by a private contractor. The private contractor determines the customs value based on a database of world prices, in contravention of international standards. Under this system, approximately 20% of all goods crossing Kazakhstan's borders are subject to valuation uplifts. While the government pays for inspections, the declaring party pays penalties in the event of discrepancies. There are concerns that this process is used to generate extralegal revenues beyond existing duties and taxes. Courts have decided over 85 per cent of all the appeals under this system against the custom agency. In addition, ministry of state revenues, order 402 sets conditional prices for certain imports a practice not is inconsistent with international norms U.S. Companies have consistently identified Kazakhstan's requirement that they obtain a "transaction passport" to clear imported goods through customs as a significant barriers to trade.

This regulation is designed to stem capital outflows and money laundering by requiring importer to show copies of contracts and other documentation to legitimize and verify the pricing of import/export transactions. The practice retards the growth of trade as the regulations place relatively tight restrictions on

[21] Foreign trade barrier, Kazakhstan http://www.ustr/gov/assets/document_library/Reports publication / 21004.

transactions parameters. For example the regulations allow a maximum financing term for imports of 120 days, after which the transaction passport must be closed out. This limits the range of business activity and creates a potential bias towards short-term financing in the economy.

Standard, Testing, Labeling and Certification

The present system of Metrology, Accreditation, standards and quality (MAS-Q) is weak and fragmented. Many businesses complain of mandatory certification requirements that have either no purpose or technical basis. The committee on standards, metrology and certification, Gosstandart (the national governing body operating under the ministry of Industry and Trade) undergoes frequent management changes that make stable, long-term progress a difficult task. Government enforcement of compliance with existing standards, testing, a labeling and certification requirement continues to be uneven. In 1999 two laws – "on standardization" and "on certification" were enacted to bring these areas into compliance with international standards and practices.[22] In 2000, the law "on ensuring uniformity of measurement" was passed.[23] In 2001, the government adopted Resolution which outlines national programs for quality for 2001-2005. These laws and the quality program are intended to bring Kazakhstan's MAS-Q system into general conformity with WTO requirements under the technical barriers to Trade and Sanitary and Phytosanitary Agreements.[24] However, there has been little progress in the implementation of this program. The law on certification requires that all imported products subjects to mandatory certification requirements be accompanied by documents identifying the producers, the date of production, the expiration date, storage requirements and the code of use in both the Kazakh and Russian. The government has accepted the placement of Kazakh language stickers on products as compliance with the law, instead of requiring

[22] ibid.

[23] ibid..

[24] ibid.

entirely new labels. The government has also issued wide ranging regulation exampling pharmaceutical products and several other categories of goods from the Kazakh labeling requirement.

Services Barriers

Foreign insurance companies are limited to operating in Kazakhstan through joint ventures with Kazakhstani companies overall capital of all foreign insurance companies do not exceed 25 per cent in the non-life insurance market. The total registered capital of banks with foreign participation is less than 25 per cent of the total registered capital of all banks in Kazakhstan. Foreign ownership of individual mass media companies is limited to 20 per cent under 2002 Kazakhstani oil and gas procurement regulations oil companies must purchase services only from Kazakhstan – based companies unless the required services is unavailable in Kazakhstan. This rule hinders the growth of external trade.

Investment Barriers

Kazakhstan's new investment law that was passed on January 2003, Supersedes and consolidates past legislation but according to major investors and law firms it is no marked improvement over the previous laws. The law has been narrowly defined in terms of investment disputes and it lack clear provisions for access to international investment arbitration and little stability and protection for contracts signed. The investment law eliminates the time limits for stability clause for the existing contracts and in some cases like oil and gas it gives precedence to sector specific legislation.

Kazakhstan has recently added a controversial, "pre-emption" amendment to its law subsurface use. The amendment guarantees the state of a right of first refusal when a party seeks to sell any part of its stake in a mineral resource extraction project. The state claims this prominent right even in cases where the controlling agreement assigns preemptive rights elsewhere (e.g., to other investors in a consortium). This amendment specifically applies the preeminent right retroactively as well. This new amendment calls into question Kazakhstan's commitment to contract sanctity. The law on subsurface use allows both citizens of Kazakhstan and foreigners to own land under commercial and non-commercial buildings including dwellings and associated lands.

Kazakh authorities often require as a part of a foreign firm's contract with the government that the firm contribute to social programs for local communities. Foreign insurance companies are limited to operating in Kazakhstan through joint ventures with Kazakhstani companies. Overall capital of all foreign insurance companies should not exceed 25 per cent of non-life insurance market and 50 percent of the life insurance market. The total registered capital of all banks with foreign participation is less than 25 % of the total registered capital of all banks in Kazakhstan.[25] Foreign ownership of individual mass media companies in limited to 20 per cent obtaining work permits for foreign investor's employees in Kazakhstan continues to be a problem. In 2001, a quota system was established that limited the number of work permits to 10500, with exceptions for investor's lead representatives. The quota is set each year based on a percentage of the total national workforce. Many companies have been complaining that the permits for key managers and technicians routinely rejected or granted for unreasonably short periods or conditioned upon demands for additional local hires. Companies also report that the regulations are confusing and interpreted differently by local officials and the ministry of labour and social protection.

Although Kazakhstan is a signatory to the New York Convention on the Recognition and Enforcement of foreign Arbitral Awards it has neither paid nor attempted to have annulled to the arbitral award that is arbitrated through the World Bank's International centre for settlement of investment disputes as provided for under the Uzbek-Kazakhstan Bilateral investment treaty.

[25] ibid.

This policy of the Kazakh government acts as a barrier to the foreign investment. There are other structural barrier to investment in Kazakhstan, including a weak business law, a lack of effective judicial process for breach-of-contract resolution and an unwieldy government bureaucracy. Many companies report significant logistical difficulties serving the Kazakhstani market. In addition there is a burdensome tax monitoring system for all companies operating in Kazakhstan. Companies are required to maintain typically large back office operations in Kazakhstan to deal with the tax system and frequent inspections. In 2001 Kazakhstan adopted transfer pricing legislation that gave tax and customs officials the authority to monitor export and import transactions in order to stop distortion of earning through manipulation of export prices.[26] This affected the foreign investments because the government rejected the use of OECD standards to determine proper market prices, creating instead a methodology that fails to account for all cost and quality differences.

Intellectual Property Rights Protection

Significant deficiencies are present in Kazakhstan's regime for the protection of intellectual property which is considered to be an obstacle in the growth of foreign trade. Due to these deficiencies, a case is pending to review Kazakhstan's status as a beneficiary country under the U.S. Generalized system of preference program. Kazakhstan has been on the special 301 watch list since 2000. The 1992 US Kazakhstan Agreement on Trade Relations incorporates provisions on the protection of intellectual property rights Kazakhstan have fulfilled a number of the agreements obligations regarding intellectual property under the agreement but several bilateral commitments remain yet unfulfilled. In 2004 Kazakhstan took steps to bring its intellectual property rights laws in compliance with the WTO agreement on trade related aspects of intellectual property rights

[26] Ibid.

(TRIPS Agreement).[27] In the same year Kazakhstan ratified the world intellectual property organization (WIPO) Copyright and performances and phonograms treaties. The Kazakh law on copy rights has also ascended to guarantee protection in for pre-existing copy righted works. In addition to legislative initiatives, Kazakhstan has worked cooperatively with law enforcement agencies, public organizations and international organizations to fight piracy. Though criminal penalties for intellectual property rights violation have been adopted in 2001 but the effectiveness of these criminal code provisions remains questionable in deterring piracy and counterfeiting due to the high burden of proof required of prosecutors. It remains unclear as to whether new criminal penalties for IPR violations will be effectively enforced and how far it will deter piracy. U.S. industry reports that it is difficult to obtain judgment in infringement cases and this serves as defacto encouragement for future trademark piracy. Though in 1999, Kazakhstan amended its customs code, to provide for the seizure at the border of items that violate IPR laws, but still illegal material, including illegal sound recording, continues to be imported particularly from Russia and China.

UZBEKISTAN

Agriculture is the most important and the largest sector in the Uzbekistan economy. Contribution in terms of the GDP, employment and export potential it is the leading sector. The development in agriculture determines the well-being of 40 per cent of the labor force, the condition for half of the industry and other sectors, the bulk of export and the resolution of key social and economic problems.[28] Since independence, Uzbekistan has undertaken the task of transforming the economy from socialist system to a market system. The task is difficult as well as very complex. Since it involve the dismantling of the old institution and restructuring the institutions to suit the need of the present. The institution of

[27] Ibid.

[28] Eskender Trushin, Uzbekistan : Problems of Development and Reform in the Agrarian Sector. Central Asia challenges of independence edited by Boris Rernser, Stanislav Zhukov.

foreign trade and trade related policies have also undergone changes in the process of economic reforms. The tasks of economic development have become ever more complex as it involves the break up of the former Soviet Union and the emergence of commonwealth of independent states. It has to build political and economic linkages on the new basis for Uzbekistan and as for the other former soviet republics.

Import Policy

The government of Uzbekistan restricts import in many ways, like high import duties, licensing requirements for importers and wholesale traders, restricted access to retail space for settlers of imported items, physical closing of borders to shuttle traders and limited access to hard currency and local currency.

According to reports from foreign investors, official tariff are combined with the unofficial, discriminatory charges resulting in total charges amounting to as much as 100 to 150 per cent of the actual value of the product, making the imported products virtually unaffordable. For example, imported liquor is reportedly subject to an excise tax of 90 per cent in contrast to an excise tax of 40 per cent to 65 per cent applied to domestic liquors. Additionally imported automobiles are subject to duties totaling approximately 150 per cent by the time they reach the consumer.[29]

The government of Uzbekistan drastically restricted imports through the imposition of official and unofficial import surcharges. It made it compulsory for the retailers to present certificates of origin and customs receipts for imported products. Otherwise the customs authorities bear the right to confisticate the goods. Survey of foreign companies consistently concluded that restrictions on access to local currency, required in order to transact business and pay employees and thus it becomes one of the worst of the many serious obstacles to do business in Uzbekistan.

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[29] http:/./w.ustr.gov/assets ubekistan, Foreign Trade barriers.

After the acceptance of the International Monetary funds' Article VIII agreement as of October 15, 2003, dramatic legislative changes took place in the country's import registration system and overall import regime. The government eliminated its import registration system, which changed the import prices and rational access to foreign exchange. But the government continued with its restriction of consumer goods imports in order to prevent hard currency flows and curbs the thread of devaluation of the Som. In addition to the official barriers, the customs clearance process is full of unofficial bureaucratic obstacles that lead to significant processing delays of two to three months, even for U.S. Uzbek joint ventures. Other problems include seizure of goods and frequent official and unofficial changes in customs procedures. Excessive documentation also makes the Uzbek importing process costly and time consuming. The lack of proper equipment and legislative regulations provide an environment in which customs officials on duty can arbitrarily make their own decisions on search and seizure procedures. The current procedures also create an intense rent seeking environment.

Standard Testing, Labeling and Certification

The system of standardization, accreditation and certification and the implementation of the sanitary and the phytosanitary (SPS) Agreement in Uzbekistan still present significant barriers to trade. According to international practice, it is very important that the mandatory application of technical regulations and standards are voluntary. Currently Uzbekistan applies mandatory technical regulations, including certain standards, which are not complaint with international practices. Uzbekistan is in the process of drafting a new law on technical regulation, which would be compliant with international system of standardization metrology, accreditation, certification and the sanitary and phytosanitary agreement.

The government of Uzbekistan accepts U.S. manufacture's self-certifications of conformance to foreign products standards and environmental restrictions. A new requirements effective as of June 2003, requires that all products be labeled in Russian and Uzbek. This is certainly a barrier to trade because of the fact that government of Uzbekistan enterprises are not held in these same standards and thus it is a kind of unequal treatment to foreign companies.

Government Procurement

Procurement decisions are made on a decentralized and adhoc basis. There is no systematic approach to government procurement in Uzbekistan. Often the procurement practices of the Central government are similar to those of many countries, with tenders, bid documents, bids and a formal contract award. A law was enacted in 2002 that created more transparency in the procurement process by mandating that all government procurement over $100,000 must be completed on a tender basis. However many tenders are announced with short deadlines and are awarded to companies that provide the most lucrative insider deals. Uzbekistan is not a signatory of the WTO Agreement on government procurement.

There are report of various case of the Uzbek government's failure to comply with contract obligations in relations to the process of procuring equipment, equipment pricing and payment guarantees. There are several cases as an U.S. company had provided equipment from a government tender and was not paid for the equipment goods.

Export Subsides

The govt of Uzbekistan give some form of export subsidy[30] to the local industries as is evident from the policy of import substitution and infant industry

[30] A subsidy to exporters, so that the price per unit received by the producers of export is higher than the price charged to foreign customers Direct export subsidies are prohibited by international agreement, but other government measure with similar effects are not uncommon. Exporters may be allowed refunds on tariff on their inputs, subsidized credit, and preferential access to ordinary credit in an economy or assistance with their capital costs or freeing cost. In economies with either currency or

protection. Export subsidies exist in the automotive sector, where local manufacturers are exempted from taxes, including value added tax (VAT), customs duties and profit tax, totaling approximately 65 per cent of their assumed profits. Export subsidy makes the domestic goods cheaper and thus the foreign goods are unable to complete in market.

Intellectual Property Rights (IPR) Protection

There are significant deficiencies in the Uzbekistan's regime for the protection of Intellectual property rights protection. In 1994 United States Uzbekistan Bilateral Trade Agreement included commitments on the protection of enforcement of IPR of which a significant number is yet to be fulfilled. As a part of effort to join the WTO Uzbekistan needs to take steps in bringing its intellectuals properly rights legislation in compliance with the WTO Agreement on trade related aspects of intellectual property rights. But yet Uzbekistan is not a member of either the Berne Convention for the protection of literary and Artistic works or the Geneva Phonograms convention. In addition to this Uzbek law does not provide for the protection of pre-existing works or sound recordings and Uzbek law does not provide adequate authority to enforce IPR violations and Uzbekistan has not yet amended its criminal code to deterrent penalties for IPR violations. And even the enforcement of IPR laws in Uzbekistan is also extremely weak. Due to this weak enforcement of law illegal optical media exports are allowed freely to cross the border for sale in Uzbekistan.

In an attempt to address the deficiencies in the IPR protection in its legal regime, the Uzbek parliament made minor changes to the Uzbek copyright law and added trademark protections in December 2000. Amendments in the 2000 session added additional protection of sound recordings but it did not cover the protections for all works and recordings. In October 2003 the govt of Uzbekistan

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direct controls on imports exporters can be allowed priority in the allocation of scare materials or foreign currency firms competing with imports which they claim have received exports subsidies may be able to obtain countervailing imports duties to offset the effects of these subsidies.

announced plans to amend a number of laws in order to bring Uzbekistan's IPR regime more close to the compliance with Uzbekistan's bilateral obligations and the requirements of the TRIPs agreement work on these laws are in progress and consultations are underway with the government of Uzbekistan so that the Uzbek IPR laws are amended consistent with bilateral and international obligations.

Service Barriers

The largest barriers to foreign services firms entering the Uzbek market is the difficulty in currency conversion. The governments have adopted currency convertibility in October 2003 to ease the process of conversion. In the past, these provisions could only be waived off by special presidential decree the grants the company the rights to do business in dollars. Till date only a state owned insurance company, Uzbek invest, established under a special presidential decree and an American-Uzbek joint ventures, Uz Aig are allowed to conduct business in dollars.[31] The government of Uzbekistan has created an insurance supervisory board, but, yet there is no system of licensing insurance companies. Therefore, the services firms can operate in Uzbekistan only on the basis of a governmental decree.

Uzbekistan imposes a less percent withholding tax on reinsurance permissions for insurers in countries that like the United States do not have a double taxation treaty with Uzbekistan.[32]

Foreign banks and insurance firms can operate in Uzbekistan only in a subsidiary in Uzbekistan only in a subsidiary capacity and the required to maintain a charter capitalization fund of $20 million.[33]

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[31] http:/./w.ustr.gov/assets ubekistan, Foreign Trade barriers.

[32] ibid.

[33] ibid.

Investment Barriers

To be considered an enterprise with foreign investment under Uzbek Law, a firm must be at least 30 per cent foreign owned and have initial foreign equity of $ 150,000. The equity is hidden through assets such as equipment or technical expertise.[34]

These capital requirements are very high and it is enough to exclude foreign investment by small companies.

Because of lack of convertibility of the Som profit repatriation is extremely difficult for foreign owned companies. The government of Uzbekistan on October 15, legally adopted currency convertibility but a case is yet to arise in which a foreign company have been allowed to convert profits into hard currency[35] for a sum larger than a few hundred thousand and dollars.

To ease the registration process of the companies the government of Uzbekistan attempted to introduces a one stop shop. These one stop shops are located in local government offices (Hokimiyets) throughout Uzbekistan. Unfortunately these new regulations have local and federal regulating road blocks that have to lead to the continuation of the bureaucratic process at a minimum of between five to ten locations.

Uzbekistan's Tax code was introduced only in 1998. It allowed no credit for VAT on capital imports, including plant, machinery and buildings. This put the firms operating in Uzbekistan at a competitive disadvantage compared to one in countries that allow such credits.

The foreign owned enterprises are subject to double taxation on their earnings. They are taxed once when earned by the enterprise in Uzbekistan and they taxed grain when remitted to the foreign parent. A significant problem in the

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34 ibid.

35 A currency which is convertibly into other currencies, and whose price in terms of other currencies is expected to remain stable, of rise. This is contrasted with a soft currency, which is not convertible into other currencies or whose price in terms of other currencies is expected to fall. Hard currencies are attractive to hold as private stores of wealth or national foreign exchange reserves.

Uzbekistan Tax code is the classification of expenses. Many expenses that are deductible for the purposes of calculating taxable profits are not deductible under the Uzbek tax code thereby increasing the effective profits tax burden in comparison to other countries.[36]

There are factor like corporate income tax rates and mandatory contribution for insurance from the payroll that increase labor cost for foreign firms in Uzbekistan. The rates are significantly higher than other similar countries. Most of the Uzbekistan companies do not comply with their tax duties but for foreign investors it in compulsory to adhere to the law. Uzbek laws are not interpreted or applied in a consistent manner. Local officials interpret the laws in a manner that in detrimental to individual private investors and business community at large.

The foreign investment law contains a number of specific protections for foreign investors but its consistent and fair application is major concern for the companies.

Other Barriers

When the business in Uzbekistan is in sectors that have either government of Uzbekistan or Uzbek-controlled firm as competitor they face increased bureaucratic hurdles and currency conversion problems. In addition to this the judiciary in Uzbekistan is not independent. In case of dispute the courts favour the firms that are either state owned on controlled by the state. Trade disputes involving foreign owned businesses are common and have proved nearly impossible to resolve in spite of the high – level intervention from senior US policy markers and legislation, bribery and other corrupt practices are common and it is another obstacle to trade. Local and international entrepreneurs face bribes from a number officials (tax, customs, police, fire / healthy / safety inspectors and labor inspectors at the local, regional and national levels.[37] These

[36] http:/./w.ustr.gov/assets ubekistan, Foreign Trade barriers.

[37] ibid.

problems are made more intense by the low salaried of the officials and opaque and cumbersome and internally contradictory legal regime that have made it difficult to do business Uzbekistan.

TAJIKISTAN

Maintaining the openness of the trading system is crucial for the country's growth strategy. The gradual substitution of the sales taxes on cotton and aluminum, and maintaining uniform and low import duties, are critical targets of the program. Following the abolition of the monitoring of export contracts by the Tajik commodity exchange, there are no non-tariff barriers in the trading system. The government trade policy is guided by the requirement for early accession to the world trade organization. The governments refrain from introducing any discriminatory tariff changes and non-tariff trade barriers inconsistent with WTO policies, and it aims to accept the obligations of Article VIII of the IMF's Articles of Agreement in the near future.[38]

Since its independence Tajikistan have develop its legislative and regulatory framework in accordance to the establishment of a market oriented economy in the country. The law on privatization of state owned property encourages the participation of foreign investors in the privatized economy. The governments of Tajikistan have signed agreements on promotion and mutual protection of investments with many countries and this is the basic structure for the regulation and framework of investment activity in Tajikistan. At present more than 210 joint ventures are established in Tajikistan. The main areas of activities of joint ventures are textiles, output of necessary products, export-import operations, agro-processing, construction and construction materials, telecommunications and mineral resources exploration. Big enterprises such as Tajik-British, "Zarafshon" and "Darnor" in the field of gold exploration, Tajik-

[38] Tajikistan, enhanced structural adjustment facility policy framework paper (1999-2000) prepared by the Tajikistan Authorities in Collaboration with the Staff of IMD and WB.

Korean "Tajik-cabool-Textiles", Tajik-American "khyannd" and Tajik-Italian "Javory" in the field of cotton processing are already operating in Tajikistan.[39]

The investment program for 1999-2001 targets the foreign direct investment in the activity like construction of water-energy-station, exploration and processing of mineral resources, cotton processing and export of textiles, production and export of citrus, processing of cattle breeding products and production of final goods, increasing the output of fertilizers, production of consumer items, reconstruction and modernization of existing agricultural capacitates, creation of programming and scientific industrial sub-sectors and development of the telecommunication system.[40]

The governments have been initiating reform since its independence. The principles and rules of the external economic activities in Tajikistan are taken by the law on Foreign Economic Activities of Tajikistan.

Tajikistan creates a quite favourable investment climate for foreign investors and it protects the right and interest of foreign investors and its economic subjects. Due to its trade liberalization it adopted the two legislative acts, which allowed the strengthening of trade economic relations of Tajikistan with the rest of the world.

In order to stimulate exports and promote foreign trade the government of Tajikistan adopted an export promotion policy. Export duties were abolished and differential rates for import duties were adopted. The accepted rates of import duties are generally lower than those in the neighbouring countries except Kyrgyzstan.[41]

For an young and sovereign nation of Tajikistan that is on its way to establish a democratic and secular state and market oriented economy. It is a fact that the processes of a accession to WTO is a long and laborious one. It requires

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39 http://www.unescap.org/tid/publication/chap3f_216opdf., p. 3.

40 ibid., p. 3.

41 ibid., p.4.

adopting many legislative acts that would conform its national legal framework to the rules and regulations of WTO. It needs the comprehensive and intensive negotiations with all other WTO members regarding the trade regimes, tariff and non-tariff measures, eliminating barriers to international trade and etc. In its process of integration of Tajikistan into the multilateral trading system more particularly WTO, it is to be remembered that this country is with a relatively small economy and limited possibilities for international trade. But it bears the potential of having major impact on international trading conditions.

In this way the accession to the multilateral trading system is very import for Tajikistan as it will give the economy protection from the discriminatory trade practices of the major trading country and the status of most favoured nation treatments of the various WTO agreements.

The benefits of the accession to WTO can be stated as – the benefits from most favoured nation treatment.[42] The advantages of the world wide the trade rules based system including the elimination of restrictive trade barriers and the discriminatory trade practices of the nations in international trade. Access to the international trade information system and this will help in analysis of the world market structures and conditions. It would enable them to develop new trade partners and have access to new market of the WTO number countries.

KYRGYZ REPUBLIC

The Kyrgyz Republic is the first CIS country to join WTO. At the same time it continues to be the member of several regional trade and economic cooperation organizations where the other participating nations are not WTO members. The need of the compulsion to comply with both the global and regional trade rule makes the foreign trade practices in Kyrgyzstan very much complicated.

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[42] A country with rights under a trade agreement. An MFN clause stipulates that imports from the partner country will be treated no less favorably than imports of similar goods from any other country . In the case of tariff, this means no other foreign goods face a lower tariff than those from the partner country with quota restrictions on trade the meaning of MFN is unclear.

The geographic factors affecting the foreign trade are its size, location, relief and climate. It is a landlocked country with infrastructure poorly developed in the eastern and southern part. In addition to the underdeveloped infrastructure is the insecure mountain going through Afghanistan which cover 90% of country's territory, arable land cover only 7% of the total area. A majority of its population is concentrated in the valleys.

Because Kyrgyzstan is a small partner in its foreign trade with the outside world it has to rely on mainly multilateral regulations that gives a common grounds for trade issued in spite of the small size of the economy.

WTO commitments of Kyrgyzstan have made its trade and investment regime liberal and it has strengthened its institutions. The commitment to WTO have made Kyrgyz Republic to abandon its protectionist policy Kyrgyz Republic have not made any attempt to protect even those sectors of the economy which are protected by many other countries of the world like agriculture, manufacturing, financial sector and telecommunication etc.

This attempt invited criticism as of being too fast in liberalizing and providing too many concessions, so the debate has been on the issue, of whether to reserve more tools for domestic market and business protection in the process of accession. The question is a difficult question to come out with a clear cut solution because it is impossible to identity sectors that would benefit in the long run from tariff or non-tariff protection. It is observed that local businessmen do not regard competition from imported goods as impediments for their activities. The real problem is not how to close domestic market from competition of foreign companies but it is how to attract more foreign investments into banking, telecommunications, tourism in etc. The recent developments in this sector (acquisition of three Kyrgyz banks of larger Kazakh ones, going privatization of Kyrgyz telecom to foreign investors, increased activity of forming of forcing investors in Issyk-Kul resort area, are perceived by the government and analysts as positive and long expected[43]. The institutional capacity of the govt also plays a important role in the protection measures. It is seen in practice that import tariff rate and the cumulative tax rate inculcating VAT, affects strongly the volume of official imports to the country but not the total import that includes a larger portion of contraband.

If the total import rate increases it means that smuggling of good have risen and that may outweigh the reduction in official imports. This reduces government revenue collections. When the nominal rate decreases there is an increase in official imports at the cost of smuggled and not domestically produced goods. This is truer in the case as excisable goods like cigarettes, alcohol and petrol. For example, in 2003 the government reduced twice the excise for gasoline and this action (paired with achieving agreement with oil Traders Association) resulted in considerable increase of official imports of oil products with no significant change in domestic demand for them.[44] Judging the scenario from this point of view the government decided not to stick to high tariffs and other protection measures and it helped to audit large distortion, smuggling and corruption. The accession provisions to eliminate tax privileges for companies are operating in Free Economic Zones and the foreign investors resulting in closing of very large gap in the legislation and the removal of one of the biggest source of distortion in Kyrgyz economy. Because of WTO accession the process of negotiations have contributed to the capacity building of the Government in foreign trade and economic cooperation as the Government was exposed to the new set of problems and issues that was never been considered earlier.

However, the trade barrier that Kazakhstan and Uzbekistan have taken up has been very harmful for Kyrgyz trade with these countries. Kyrgyzstan's exchange rate controls, impediments for inter-country payments, cross-border trade and movement of people (with regard to trade with Uzbekistan) and

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43 Roman Mogilevsky, Role of Multilateral and Regional Trade Discipline, http://www.case.com.p. l

44 ibid., p. 16.

prohibitively costly procedures of transit through territories of Kazakhstan and Uzbekistan.[45] The joint membership of Kazakhstan, Kyrgyzstan and Uzbekistan failed to remedy these problems. The regional agreements either do not consider the problematic areas or it has special reservation that allows countries to effectively impede trade with the other agreement signatories.

Russia and Kazakhstan are the first and second large non-gold and non-electricity export market for Kyrgyzstan and main absorbers of Kyrgyz agriculture produce (cotton, tobacco, vegetable, fruits), consumer materials, and machinery. All these commodities are very sensitive to transportation cost and have become primary victims of trade barriers on Kazakh side Trade with Uzbekistan suffers from still remaining barter arrangements when Uzbek natural gas is exchanged for Kygyz electricity / water and some other commodities. The share of non energy commodities trade turnover is shrinking from 50% in 1996 to 29% in 2002. In 2002-03 the situation in trade with Kazakhstan and especially with Russia started to improve. The economic growth and large inflow of oil dollars to these countries resulted in emergence of large companies, which started to expand their activities in neighbouring countries including Kyrgyzstan. FDI from Russia and Kazakhstan to Kyrgyz industrial, tourism and banking sector are increasing during last years. The increase contributes both to growth of exports to and imports from these countries. Growth in export of services (tourism in Issyk-Kull area) is also visible. Establishing of closer economic companies helped to resolve out of the most acute problems o Kyrgyz foreign trade.[46] Kyrgyzstan hoped that joining WTO it would attract for forcing investors. But one of the larger disappointments related to the WTO accession was the FDI dynamics. When China entered WTO Kyrgyzstan had the possibilities being the only window into Chinese market among the CIS countries. But it did not materialize as such; in 2000-2001 FDI flow fell by one third in comparison to 1998 level.

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[45] ibid.

[46] ibid.

CHAPTER – 3

FOREIGN TRADE REGIME AND FOREIGN TRADE STRUCTURE

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Foreign trade structure of an economy deals with the pattern of the trade, exports, exports composition, imports composition and the trading partners. Foreign trade structure of a country reflects its stage of economic development, its political, social and other background since trade is governed by its polity, economy and other related aspect. Trade regime generally deals with the policies of export and import, policies regarding tariffs, customs, quantitative barriers, exchange rate, trade related intellectual property rights and policies regarding direct foreign investment and port folio investment, policies regarding import and export subsidies etc.

The Foreign trade regime and foreign trade structure are highly interrelated, as one is dependent on the other. In this chapter an attempt has been made to describe the structure of trade and the trade regime in the five Central Asian Republic. The description is given country wise covering the major issues of the existing trade regime. The structure of trade is been represented with the help of figure and tables. In every section the last part deals with the prospect of the economy in the background of WTO. The first part deals with the foreign trade of Central Asia as a whole.

Questions about the role of trade and trade policy in development, represent one major influences on generalization made about macroeconomic polices and the development strategy to be pursued by the economy. One area where the influence is manifested is the choice between import substitution and export promotion strategy and this debate is a debate between structuralist[1] and

[1] The best-known brand of development economics that arose in the 1950s is called the structuralist school. Unlike neoclassical economists, who assumed a smoothly working market-price system, some of the early development economists adopted a more structuralist approach to development problems

neoclassical[2] school. These schools have expressed divergent views on the role of trade in economic development.

Central Asian Economies in their stages of transition towards liberalization and privatization faced with similar dilemmas. Since the Days of central planning are over, these five Central Asian economies in their process of economic reform have taken globalization as their goal therefore they are going for liberalization of their respective economies. Therefore they are relying more on market forces which is a shift from the state controlled central planning economy. As a part of the globalization policy of export promotion has gained more and more importance and the merits of import substitution have reduced in importance. These republics have been making or intend to make efforts to restructure foreign trade policy and boost their foreign trade.

The economies differ in their trade structure as well as the trade policies, based on their initial condition and geographical factors and other related factors[3]. Recently the entire trade structure stands under transformation because of the disintegration of the former Soviet Union. In this scenario the foreign trade

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where they adopted a more pessimistic view about the ability of the free market to eradicate poverty. Economists such as Gunnar Myrdal, Raul Prebisch, and Hans Singer were especially prominent in questioning the possibility of development through export of primary products. Immediately after independence the prevailing neo-classical doctrine on development of poor countries emphasized three elements: (1) a massive dependence on private foreign investments, (2) each nation to build on its existing comparative advantages, and (3) a continued emphasis on export of primary products. Shortly after the Second World War Presbisch and Singer working separately published research results that were critical of that conventional wisdom, a concept that has since come to be called "the Prebisch-Singer thesis." They announced that over time poor countries have experienced deteriorating terms of trade in their dealing with industrial countries, meaning they have to export more of their primary products just to maintain their previous level of imports of manufactured goods. This is called the deteriorating terms of trade. Available at http://www.geog.psu.edu/courses/geog103/neoliberalism.htm

2 This approach in economics of analyzing how individual and firm should behave to maximize their own objective functions assuming that activities are coordinated by the price mechanism and that market clear so that the economy is in equilibrium at all times. *A dictionary of Economics* Great Clare don street, Oxford University Press 1997 p.318

3 Since Soviet regime each area was developed as specialized region for some particular economic activity. For example fertile plain of Uzbekistan was developed as heart land for cotton cultivation. Each economy was specialized but not diversified so after the break down of soviet they are facing serious problems and their export and import differs.

policies has gained increasing importance. This chapter makes an attempt to view the foreign trade regime and existing trade structure.

All five of the Central Asian countries which became independent in late 1991 are economies that export, primary products. Central Asian countries want to diversify their exports in this effort all of them declared their intention to participate in the global trading system. They have, to varying degrees, pursued trade policies incompatible with WTO rules and have, with the exception of the Kyrgyz Republic, been cautious about accepting the obligations imposed by WTO membership. At the same time they have all signed on to myriad regional agreements which might threaten adherence to the most-favored nation principle at the heart of the WTO-based system. The failure of the many preferential trading agreements mooted since 1992 should have already clarified that they are not a practical route to realizing greater gains from trade[4].

Despite many proposals for regional trading arrangements, in practice the Central Asian countries have in their trade policies clearly chosen the path of policy autonomy combined with non-discriminatory multilateralism. Buying imports from the global least-cost supplier and selling exports in the best market makes considerable economic sense, and is supported by the failure of the many discriminatory trading arrangements in Latin America and Africa during the second half of the twentieth century (Pomfret, 1997/2001).

The success of the European Union is a red herring insofar as on the political level the EU has been the vehicle for closer political ties, whereas the Central Asian countries have broken earlier political ties and have no wish to compromise their political autonomy now, and on the economic level the least-cost EU producer's price will generally be little different from the world price[5].

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4 Richard Pomfret. Trade Policies in Central Asia after EU Enlargement and before Russian WTO accession: Regionalism and Integration into the world economy. Working Paper 2004-13School of Economics University of Adelaide University, 5005 Australia available at www.econwpa. wustl.edu.8089\eps\othr\paperso\0502\0502003.pdf

5 There are exceptions to this, e.g. in agriculture and in clothing, but the EU appears willing to accept the trade diversion in these sectors. Even allowing for such exceptions, the potential trade diversion

The positive feature of the Central Asian countries' *de facto* multilateralism is that the region remains well-placed to take advantage of opportunities offered by China's recent WTO accession and Russia's imminent accession.

Central Asian countries which are or become WTO members will benefit from a rule-based environment in their trade with all neighboring economies except Afghanistan, and rules which are generally the most desirable for small open economies. The costs in terms of restrictions on import-substitution strategies and other anti-liberal trade policies and in terms of reduced potential for political grandstanding via economic proposals in regional foray are minor – and indeed the tying of governments' hands in Comments like "The heads of the CIS states have all met regularly, but the agreements drawn up at their meetings have had no real force" and "most of the employees of the CIS, who at one point numbered about 2,500, were essentially wasting their time" (Olcott, Aslund and Garnett, 1999, 3 and 10) apply to all the organizations listed in (Table 5). There are exceptions to this, e.g. in agriculture and in clothing, but the EU appears willing to accept the trade diversion in these sectors. Even allowing for such exceptions, the potential trade diversion associated with potential preferential trading arrangements among the Central Asian economies is much higher due to their similar economic structures and generally uncompetitive manufacturing sectors. Such activities should benefit the countries' citizens. Additional benefits from WTO membership include a possible reform-reinforcing effect, as well as access to the WTO dispute resolution mechanism and the ability to join coalitions working towards reducing trade barriers facing important exports. Yet, there are benefits from regional cooperation in Central Asia, and if these could be realized that would help to defuse political tensions. In water resource management the potential benefits are obvious and enormous. In preventing terrorism the benefits

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associated with potential preferential trading arrangements among the Central Asian economies is much higher due to their similar economic structures and generally uncompetitive manufacturing sectors.

from regional cooperation are real but may be manipulated to restrict liberty. Regional cooperation in trade facilitation and in transit arrangements could reduce the tragedy of the anti-commons, where people promoting self-interested goals are choking off trade that would be mutually beneficial. This tragedy can be mitigated by government actions to discourage or regulate anti-social behavior by local authorities, customs officials and others under their jurisdiction. The national governments can also benefit by implementing policies to reduce other impediments to trade such as cumbersome visa regulations, poorly developed financial systems, and capricious changes in border crossings, but that requires an appreciation that many of the foregone trade opportunities represent win-win situations. What are the prospects for improved international economic relations in Central Asia during the first decade of the twenty-first century? At the institutional level, existing regional organizations have been strengthened, at least on paper, as the Union of Five became the Eurasian Community, the Shanghai Forum became the Shanghai Cooperation Organization and the Central Asian Economic Community was succeeded by the Central Asian Cooperation Organization. Whether the implementation ability of the new organizations will exceed that of their predecessors remains uncertain. The events of September 2001 stimulated declarations of concerted action against terrorism, but the immediate consequence was to widen the fissure between the Eurasian Community members and the countries which are more skeptical about Russia's role in the region. Moreover, recent developments within the region, especially increased territorial disputes, are creating a climate which is inimical to cooperation. Whether justified on security grounds or not, new border control measures are unpopular among the local populations who have no history of such restrictions, and as assertions of the new states' territorial rights they augur poorly for inter-state cooperation. On the specific question of the choice between regionalism and multilateralism in trade relations, the verdict from Central Asia is clear-cut. Regionalism may appear attractive, but on deeper investigation preferential regional trading arrangements are unattractive. Multilateralism formalized by WTO membership may look like an unattractive restriction on policy autonomy, but on deeper investigation is the best framework within which the Central Asian countries can develop their international economic relations.[6]

Table 5: Membership of Regional Agreement involving Central Asian Countries

	CIS	Eurasian Com.	UES	CACO	SPECA	ECO	SCO
Kazakhstan	x	x	x	x	x	x	x
Kyrgyz Rep	x	x		x	x	x	x
Tajikistan	x	x		x	x	x	x
Turkmenistan	x				x	x	
Uzbekistan	x			x	x	x	x
Russia	x	x	x				x
China							x
Iran						x	
Pakistan						x	
Turkey						x	
Afghanistan						x	
Azerbaijan	x					x	
Armenia	x						
Belarus	x	x	x				
Georgia	x						
Moldova	x						
Ukraine	x		x				

THE CENTRAL ASIAN COUNTRIES' TRADE PATTERNS AND POLICIES

The five Central Asian countries' trade patterns changed substantially over the 1990s, although the precise magnitudes are uncertain due to the variable quality of the trade data. Especially in 1992 and 1993 when the region was using a common currency, trade within Central Asia and with important trading partners such as Russia and Ukraine went largely unmonitored. Even after the

6 ibid

establishment of national currencies and of functioning national customs services, the coverage of official trade statistics remained far from complete. Small-scale traders (referred to as shuttle traders in the region) account for a large amount of imported consumer goods and other trade, but the recording of this trade is uneven.[7] Illegal trade is also important with widespread smuggling and with the Afghanistan-originating drug trade passing through Tajikistan and the Kyrgyz Republic and through Turkmenistan. After the major shocks of the early 1990s, trade recovered in the Central Asian countries in 1994-7. According to official import and export data reported by the IMF (Table 6).

Table 6: Total Exports and Important, 1993-2002 (millions of US dollars).

	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002
Exports										
Kaz.	1,107	3,227	5,256	5,926	6,497	5,511	5,598	9,138	8,647	9,930
KR	360	339	483	506	609	509	454	502	476	480
Taj	350	492	749	772	803	597	689	784	652	537
Tkm	561	1,163	1,881	1,693	751	594	1,187	2,505	1,132	1,219
Uzb	693	1,991	2,718	2,620	2,896	2,310	1,963	2,135	2,028	1,900
Imports										
Kaz.	1,704	3,285	3,807	4,247	4,302	4,373	3,686	5,052	6,363	6,809
KR	447	316	392	795	709	841	610	554	464	593
Taj	532	547	810	668	750	711	663	675	688	705
Tkm	586	904	1,364	1,313	1,228	1,007	1,478	1,788	1,558	1,432
Uzb	918	2,455	3,030	4,854	4,538	2,931	2,481	2,078	2,303	2,370

Source: Elborgh-Woytek (2003, 4 and 5), based on IMF *Direction of Trade Statistics*.

[7] Pomfret (1999, 32n) reports official estimates from Kazakhstan of shuttle trade accounting for a quarter of total imports in 1995, a third in 1996 and over four-fifths in 1997. It cannot be assumed that official data understate trade by a constant percentage, because the share of informal trade varies across countries and across periods. Uzbekistan's vibrant bazaars and shuttle trade were brought under tighter state control and heavily taxed in 2000-1 ostensibly to protect consumers from shoddy imported goods, but whether this reduced the small traders' activity or simply pushed it further underground is uncertain.

In both the Kyrgyz Republic and Tajikistan, per capita values remained small and declined after a 1997 peak. The relatively superior export performance of Kazakhstan and Uzbekistan in the mid-1990s was due in part to favorable energy and cotton prices and their divergent experience after 1997 is partly explained by the drop in world cotton prices since 1996 and booming oil prices since 1999. Turkmenistan's exports are dominated by energy products and the 1995-6 values are inflated by over-reporting of natural gas exports to CIS destinations which were not paid for (the invoice value was recorded as exports, while the accumulating payment arrears were recorded as foreign assets); recognizing that the bills would never be paid in full, Turkmenistan stopped supplying gas in March 1997, after which export values (and GDP) collapsed until the flow was resumed in March 1999.[8] (Table 7) presents Islamov's reconstruction of trade shares by destination. The initial values illustrate the overwhelming orientation to former Soviet markets at the start of the 1990s. By 1996 over half of the Central Asian countries' international trade was with non-CIS countries (Kaser, 1997, 179). The lead was taken by Uzbekistan, and reflects primarily the ability to sell cotton on world markets[9].

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8 Turkmenistan's economic data are the least reliable in the CIS. According to other sources (reported in Pomfret, 2001, 158), gas exports fell from about a billion dollars in 1996 to $70 million in 1997, andthis coincided with a poor cotton harvest due to which cotton exports fell from $332 million in 1996 to $84 million in 1997.

9 Breaking non-CIS trade down by country is not very interesting, because most exports went to cotton exchanges in the UK or Switzerland from whence the final destination was unknown (and of little concern to Uzbekistan). Kazakhstan's oil also becomes anonymous once it leaves the country; in2002, according to the IMF *Direction of Trade Statistics*, over a fifth of Kazakhstan's exports went to Bermuda.

Table 7: Share of Exports and Imports with the CIS, 1991-9 (percentages)

	1991		1992		1993		1994		1995	
	X	M	X	M	X	M	X	M	X	M
Kazakhstan	91	86	88	94	84	90	58	61	53	69
Kyrgyz Rep	97	80	94	96	88	91	66	66	66	68
Tajikistan	78	82	80	90	53	62	19	43	34	59
Turkmenistan	95	79	80	85	70	78	77	47	49	55
Uzbekistan	84	82	83	86	74	81	62	54	39	41

	1996		1997		1998		1999	
	X	M	X	M	X	M	X	M
Kazakhstan	56	70	46	54	40	47	26	43
Kyrgyz Rep	78	58	53	61	45	52	40	43
Tajikistan	43	57	36	64	34	63	46	78
Turkmenistan	68	30	60	55	26	47	na	na
Uzbekistan	21	32	33	27	25	28	30	26

Source: Islamov (2001, 173).

The other large country, Kazakhstan, was slower to diversify markets, unsurprisingly given its reliance on oil pipelines and mineral-processing links and its proximity to Russia, but the CIS share of Kazakhstan's trade had fallen to half in 1997 and dropped substantially further in 1999 during the export boom following devaluation of the currency[10]. Only Tajikistan remains significantly dependent on CIS suppliers, and this largely reflects geopolitical and military considerations as unrequited imports are provided by Russia and Uzbekistan. The Central Asian countries' tariff schedules have, in general, been fairly liberal (Table 8) and without great variance, although this has not been consistently true.

[10] Richard Pomfret Trade Policies in Central Asia after EU Enlargement and before Russian WTO accession: Regionalism and Integration into the world economy .Working Paper 2004-13School of Economics University of Adelaide University, 5005 Australia available at www.econwpa.wustl.edu.8089\eps\othr\paperso\0502\0502003.pdf

Table 8: AVERAGE IMPORT TARIFF 2002(percent)

Kazakhstan	7.9
Kyrgyz Republic	5.2
Tajikistan	8.3
Turkmenistan	0.5
Uzbekistan	19.0

Source: IMF data reported in World Bank (2004, Table 3.2).

The Kyrgyz Republic has bound most tariffs at ten percent as part of commitments made during WTO accession negotiations, and actual tariffs in 2002 averaged half of this level. Kazakhstan also has had a liberal trade policy since mid- 1996, when export duties were removed and the average tariff on imports fell to twelve percent; the average tariff had fallen below eight percent by 2002, but there are recurring complaints of *ad hoc* impositions which make trade policy less predictable. Uzbekistan's July 1995 tariff schedule had an average tariff of eighteen percent, but included some high rates[11]. Both Turkmenistan and Tajikistan also levy protective tariffs as well as imposing a range of export restrictions (mainly in the form of surrender requirements on foreign exchange earnings). Episodes of illiberal policies have involved tariffs, non-tariff barriers to trade, and restrictions on access to foreign exchange. Uzbekistan in 1996 and Turkmenistan in 1998 responded to balance of payments difficulties by reintroducing foreign exchange controls, which made other import restrictions largely irrelevant[12].Kazakhstan suddenly raised duties on intra-Central Asian trade

[11] Uzbekistan had applied duties of up to one hundred percent on automobiles to protect the UzDaewoo joint venture.

[12] The Kyrgyz Republic, in March 1995, and Kazakhstan, in July 1996, have accepted Article VIII commitments to the International Monetary Fund, guaranteeing full current account convertibility and non-discriminatory currency arrangements. In early 1996 Uzbekistan had committed to formally adopting Article VIII, and its currency was *de facto* convertible, but the commitment was abandoned and controls introduced in the second half of 1996. Although frequent declarations of intent were announced in the late 1990s and early 2000s, the introduction of currency convertibility was delayed until October 2003. Turkmenistan made circulation of foreign currencies illegal in December 1995, although the small private sector had reasonable access to foreign currency and the official and curb rates were close together until the second half of 1998, when tight exchange controls were introduced.

in response to its 1998 crisis[13] . Border crossings have been temporarily closed, and, because such actions are often unpredictable, they may be discovered only upon arrival at the border. Customs officials operate with considerable discretionary power, and bureaucratic requirements impose substantial costs (especially for importers into Uzbekistan since the removal of exchange controls late in 2003). In October 1999, Kazakhstan passed legislation requiring labeling of all imports in both Russian and Kazakh, which could become a significant non-tariff barrier, although its implementation has been postponed. In Tajikistan, the central government does not exert physical control over the entire national territory, and it has lost control over some border regions for lengthy periods.

Actual collected customs duties have often been less than legislated tariffs. In the initial post-independence years borders within the former Soviet Union were lightly policed, and goods crossed with little regulation. In addition numerous preferential trading arrangements among the Central Asian countries or with neighbors both within and outside the former USSR have been signed, although these appear to have been rarely implemented. Gap is widening as the country rides an oil boom driven by new discoveries as well. In sum, with all the reservations noted in this section, the Central Asian countries are open economies. The two countries with the most restrictive barriers to trade, Turkmenistan and Uzbekistan, are necessarily trading nations because they have such obvious comparative advantages in natural gas and in cotton. The Kyrgyz Republic and

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13 After the August 1998 Russian crisis, which hit Kazakhstan hardest among the Central Asian countries, Kazakhstan introduced a 20% value-added tax on all personal imports from Russia, the Kyrgyz Republic and Uzbekistan, and then in December 1998 enacted a law on "Measures to Protect the Domestic Market from Imported Goods". Under this law, special tariffs as high as 200% were imposed on a number of goods imported from the Kyrgyz Republic and Uzbekistan in February 1999, when a number of other restrictions such as import quotas on cement imports from the Kyrgyz Republic were also introduced. In April 1999 the 200% February tariffs were eliminated, but new licensing procedures, transit fees and mandatory deposits on imports from the Kyrgyz Republic and Uzbekistan were introduced and the Kazakh tenge was floated, which led to an effective fifty percent devaluation. Also in early 1999, Uzbekistan tightened its foreign exchange controls and introduced a 5% tax on all purchases of foreign exchange. Turkmenistan closed the commercial banks' foreign exchange window in December 1998, and enacted legislation requiring all export and import contracts to be approved by the State Commodity Exchange.

Tajikistan are open in terms of low trade barriers, but the volume of their international trade is limited by their relative resource scarcity and by their landlocked status and difficulty of transiting neighbors. Kazakhstan is the biggest trading nation, and the as high world oil prices[14].

WTO STATUS

All the Central Asian countries have shown their desire and willingness to join the WTO as they are of the view that such membership shall eventually bring economic benefits for these countries. But the conditions and requirement of WTO membership pose a particular problem for these countries.

The economic structure, economic regulations and economic policies of these countries are not in tune with the conditionalities, rules and regulations framed by the WTO for countries to adhere in order to become its members.

The most important benefit of WTO membership would be to place all Central Asian trade on a common basis of international trade law, and potentially to separate trade from politics. Kazakhstan's WTO accession has long been expected to be closely tied to that of Russia, due to the strong economic links with its northern neighbor[15]. Pressure would then be on Tajikistan and Uzbekistan to accelerate their accession negotiations. The Central Asian countries' accession would provide a common framework for formal trade policies and dispute resolution with respect to both intra-regional trade and trade with all of the region's economically important neighbors[16]. Overall, the trade performance of the Central Asian countries has been disappointing and below potential. Apart from

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14 Richard Pomfret Trade Policies in Central Asia after EU Enlargement and before Russian WTO accession: Regionalism and Integration into the world economy. Working Paper 2004-13School of Economics University of Adelaide University, 5005 Australia available at www.econwpa. wustl.edu.8089\eps\othr\paperso\0502\0502003.pdf

15 A major agenda item at the Eurasian Community's May 2002 Moscow summit was coordination of the WTO negotiations by Russia, Belarus, Kazakhstan and Tajikistan. The Kyrgyz Republic has been threatening to withhold consent for Kazakhstan's accession until unresolved transit issues are settled, but that is unlikely to be an insuperable obstacle.

16 Iran, Pakistan and Turkey, are all WTO signatories

Kazakhstan's oil-driven post-1999 boom, the Central Asian countries' export growth since 1994 has been mediocre. The explanation is a mixture of the destruction of intra-CIS trade due to the erection of borders, and the failure to realize the potential for trading in the major non-CIS markets. One indicator of the potential for international trade is the contrast between intra-Russian trade and international intra-CIS trade. Using a gravity model, Djankov and Freund (2002) estimate that trade among Russian provinces is around sixty percent higher than trade between CIS countries, *ceteris paribus*; this suggests the large orders of magnitude by which the Central Asian countries' trade could increase if the size of the border effect could be reduced. In World Bank (2004, 8), the actual trade flows are compared to those predicted from a gravity model of world trade flows; in 2001 all five Central Asian countries still traded more than predicted with CIS countries, and they mostly traded less than predicted with the EU, USA and China[17]. Clearly such estimates are no more than indicative in what remains a disequilibrium situation, but they suggest the potential benefits from reducing the costs of conducting international trade and facilitating access to the major world markets. The lack of a stable institutional environment for international trade is part of the high costs of doing trade with Central Asian countries, and WTO membership could alleviate these costs. WTO accession could bring further benefits by encouraging liberal policies and punishing backsliding on commitments. Such an environment would help to attract foreign direct investment, as well as making domestic investment more attractive. With a positive domestic environment, WTO membership helps to ensure that a country can reap benefits from specialization and trade with diminished fear of protectionist responses in foreign markets. Finally, WTO membership would grant some leverage to reduce existing illiberal polices. Most immediately, Uzbekistan and Tajikistan would want to join WTO member countries lobbying for reduced

[17] The only exceptions to this last generalization are that Kazakhstan and the Kyrgyz Republic traded more than predicted with the EU and with China.

subsidies to cotton producers in the USA and EU[18]. Four West African countries have had success in publicizing the harmful impact of these subsidies on some poor countries' export earnings, and they formally introduced the Cotton Initiative into the Doha Development Agenda in April 2003 (Sumner, 2004). In October 2004 Brazil obtained a WTO ruling that some government subsidies to US cotton producers are illegal, and that case will spend the next year under appeal. Central Asian cotton-producing nations would broaden the coalition and highlight the iniquity of subsidizing rich country farmers to the detriment of poor farmers in areas with a comparative advantage in growing cotton[19].

Only The Kyrgyz Republic among the Central Asian countries has joined the World Trade Organization (WTO) which did in 1998 Kazakhstan's application appears to be fairly far-advanced. Uzbekistan's accession process is at an earlier stage than Kazakhstan's. Tajikistan applied for WTO membership in 2001. Turkmenistan has not made an application[20].

The Kyrgyz Republic was the first Central Asian country to apply for WTO membership. Given its liberal trade policies, including a low and even tariff structure and few non-tariff barriers, negotiations went smoothly and the country became the first former Soviet republic to join the WTO. In the transition country context, the Kyrgyz Republic was typical of a number of small countries with

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18 Direct assistance to cotton growers amounted to $2.3 billion in the USA and $0.8 billion in the EU in the 2001/2 season. Baffes (2004) estimates that these subsidies raised producer prices above the world price by 91% in the USA, by 144% in Greece and by 184% in Spain; the domestic supply response to these artificially high prices lowers world prices, and removal of the US and EU subsidies would increase world prices by as much as 71 percent.

19 The cost to Central Asia of the subsidy-induced lowering of world prices is large. With world cotton prices 71% higher, the gain in export revenue would have added 3% to Uzbekistan's GDP, 6% to Tajikistan's GDP and 3% to Turkmenistan's GDP in 2000, even without any change in their output (Pomfret, 2004). These substantial benefits would accrue every year after abolition of the subsidies Moreover, with more attractive world prices, the quantity of cotton exported would increase (by 5.8% in Uzbekistan according to Baffes's estimates), adding to the potential benefits.

20 For more details on the Central Asian countries' WTO relations, see Pomfret (2003) and Michalopoulos (2003).

liberal policies whose accession negotiations were untroubling to existing members[21].

Uzbekistan was the second Central Asian country to apply, and the Working Party on the accession of Uzbekistan to the WTO was established in December 1994. This was during a period of substantial reform of the Uzbekistan's economy which had been initiated in January 1994 with a purposeful macroeconomic stabilization package. The reforms, however, began to lose momentum and were substantially undermined by the reintroduction of rigid exchange controls in October 1996. The

Reform slowdown was reflected in snail's pace progress through the WTO accession process. Uzbekistan submitted its Memorandum on the Foreign Trade Regime in September 1998 and replies to questions were circulated in October 1999. The first meeting of the Working Party took place on 17 July 2002. The October 2003 reforms, which included establishment of currency convertibility, may signal a change of direction which could accelerate the accession process. Kazakhstan's Working Party was established in February 1996. Bilateral market access negotiations in goods and services commenced in October 1997, and are continuing based on revised offers in goods and services. The process slowed down in 1998 following the Russian Crisis and its contagion effects on Kazakhstan, but has been revitalized since 2001[22]. In May 2001 Tajikistan lodged a formal request for accession. A Working Party was established at the WTO General Council meeting in July 2001. Tajikistan has not yet submitted a

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21 Slovenia joined the WTO in 1995, Bulgaria in 1996, Latvia and Estonia in 1999, Georgia, Albania and Croatia in 2000, Lithuania and Moldova in 2001, Armenia in 2003.

22 Topics under discussion in the Working Party include agriculture, the customs system (and customs union arrangements), price controls, import licensing, industrial subsidies, sanitary and phytosanitary measures (SPS) and technical barriers to trade (TBT), transparency of the legal system and legislative reform, services and intellectual property rights (TRIPS). The common belief is that, because of the Kazakhstan economy's close trade links with Russia, Kazakhstan's WTO accession will follow very soon after that of Russia.

Memorandum on the Foreign Trade Regime, and the Working Party has not yet met[23].

Table 9: Status of WTO Accession Negotiations

	Applied	Working Parties	Member
Kazakhstan	January 1996	6 meetings 1997-2004[a]	
Kyrgyz Rep.	1993		December 1998
Tajikistan	May 2001	WP not yet met	
Turkmenistan	Not applied		
Uzbekistan	December 1994	1 meeting, July 2002	
China	1986		December 2001
Russian Fed.	June 1993	19 meetings, 1995-2003[b]	

Source: WTO website.
Notes: a - Kazakhstan Working Parties met on 19-20 March 1997, 9 October 1997, 9 October 1998, 13 July 2001, 15 July 2003, and 4 March 2004.
b - Russian Working Parties met on 17-19 July 1995, 4-6 December 1995, 30-31 May 1996, 15 October 1996, 15 April 1997, 9-10 December 1997, 29-30 July 1998, 16-17 December 1998, 25-26 May 2000, 5 December 2000, 26-27 January 2001, 26-27 June 2001, 23-24 January 2002, 25 April 2002, 20 June 2002, 31 January, 6 March, 10 April and 10 July 2003.

TRADE STRUCTURE AND TRADE REGIMES OF INDIVIDUAL CENTRAL ASIAN REPUBLICS

TURKMENISTAN

Although slow to begin the reform process, Turkmenistan's steps towards macro-economic restructuring aim to improve the business and investment climate. In December 1995, President Niyazov unveiled the "President's Programme for Social and Economic Development in Turkmenistan", an IMF-recommended programme. The Government is voluntarily implementing this programme. Turkmenistan does not qualify for the IMF standby agreement

[23] Richard Pomfret Trade Policies in Central Asia after EU Enlargement and before Russian WTO accession: Regionalism and Integration into the world economy. Working Paper 2004-13School of Economics University of Adelaide University, 5005 Australia available at www.econwpa.wustl.edu.8089\eps\othr\paperso\0502\0502003.pdf

because it does not have a balance of payments problem. Key objectives of the economic reform programme include strengthening and implementing market reforms, making the national currency, the manat, internally convertible, and restructuring the economy[24]. Principal reforms focus on controlling the expansion of credit, managing budget deficits, and liberalizing foreign exchange[25]. Turkmenistan in its process of economic reform is trying to diversify its export and liberalize its economy in order to meet the challenge of the changing global order. In this section first the export import structure of its trade and then the trade regime is described.

Foreign Trade structure

Exports

Turkmenistan's exports depend heavily upon three products: natural gas, cotton, and oil products. After running a chronic trade deficit with the rest of the former Soviet Union prior to independence, Turkmenistan began posting a trade surplus in 1991 as a result of higher gas export prices. Gas export revenue grew during the early 1990s and made up more than 60 per cent of total export earnings in both 1995 and 1996 (although changes in recording practices registered a fall in gas exports in 1996). Turkmenistan's extreme reliance on gas exports plunged the economy into difficulty when gas exports were suspended in March 1997. The country's traditional trade surplus turned into a massive trade deficit in both 1997 and 1998. Gazprom, the Russian state-controlled gas monopoly, has played a major role in limiting Turkmenistan's gas export market. As a result, Turkmenistan had been required to turn to alternative markets in Ukraine and Transcaucasia. However these countries have not been able to pay on time nor to pay the $ 80 per 1,000 cu meters originally demanded by Turkmenistan. As a result, Turkmenistan received payment for just over 50 per cent of gas exports in

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[24] http://www:unescap.org/tid/publication/chap3g_2160.pdf

[25] Based on a paper prepared by Mr. Mehrdadhaghayeghi *Country papers on accession to the WTO* available at :www.unescap.org/tid/publication/chap3g_2160.pdf

1993 and 1994 and for just under 75 per cent in 1995, the same year in which the price charged to Ukraine dropped to $ 42 per 1,000 cu meters. Even though most of this trade occurred on barter terms, late payment remained endemic. The IMF estimated that by the end of 1996 the total value of gas payments arrears and debt owed to Turkmenistan had reached $ 1.6 bn, equivalent to 76 per cent of GDP and larger than Turkmenistan's external debt of $ 668 m. Only 9 per cent of gas exports were paid in cash in 1996. The proportion of gas export receipts collected dropped to just 66 per cent in 1996, sparking a dispute with Gazprom and with Turkmenistan's supply intermediary, Itera International Energy (US), and ultimately causing the suspension in exports that occurred in March 1997. Exports to Ukraine resumed only in, January 1999, when Turkmenistan, Ukraine and Gazprom finally agreed upon a price of $ 36 per 1,000 cu meters. Just 40 per cent of the amount was to be settled in cash. Even this proved too much for Ukraine, which accrued considerable arrears during the first months of the new agreement and requested a renewed suspension in May 1999[26].

Problems with Exports

Turkmenistan will eventually need to offer foreign companies equity in gas sector in order to make any gas pipelines commercially attractive. Without foreign equity participation, financing will prove elusive. Unlike oil, this can easily be sold in the market at the spot. Turkmen gas exports that require long-term contracts. Turkmenistan has so far failed to secure access to markets and unable to pay reasonable prices promptly. Moreover, Turkmenistan's distance from these potential market results in substantial transit fees and, consequently, lower net export earnings. For instance, Turkmenistan needs to offer foreign companies equity in the gas sector in order to Ukraine pays $ 68 per 1,000 cu meters for the gas on its border with the Russian Federation, of which Turkmenistan receives only $ 36 in export revenue – the rest being accounted for by transit fees. Turkmenistan's

[26] http://www.unescap.org/tid/publication/chap3g_2160.pdf

distance form its two largest potential non-CIS export markets, Pakistan and Turkey, combined with the cost of building export pipelines, would similarly result in a gas export price far below the $ 80 per 1,000 cu meters originally sought by the President. The value of oil exports increased by 2.5 per cent in 1996[27], which reflected a low increase in crude oil production (0.7 per cent), and possibly an increase in domestic demand[28].

Most of the oil exports are to non-CIS markets[29]. Despite the Government's policy of eliminating barter trade in oil, only 35 per cent of oil exports were paid for in cash, although this constituted a significant improvement over 1995, when only nine per cent of oil exports were paid for in cash. The agricultural sector provides much greater export potential, although poor agricultural policies and bad weather have depressed Turkmenistan's cotton export receipts. The most recent figures indicate that the disastrous cotton crop of 1996 caused an almost 75 per cent fall in cotton exports, from $327m to $84m in 1997. Unlike gas exports, Turkmenistan's cotton exports are predominantly paid for in hard currency. In 1997, for instance, Turkmenistan received hard-currency payments for all of its cotton exports and for none of its gas exports. Hoping to capitalize on this, the Government has tried to attract investment into the textiles sector in order to increase the value added of Turkmen cotton exports. Outside the state sector, Turkmenistan has little export potential at the moment, given the exclusion of the small private sector from any export opportunities. Electricity exports provide an alternative potential cash earner, but have suffered from Kazakhstan's inability to pay and that country's efforts to build its own electricity industry. Turkmenistan also exports electricity to Tajikistan. Similarly electricity exports to Tajikistan have suffered from payments problems. In the first six months of 1996,

27 Turkmenistan refines all crude oil production and exports only refined products

28 http://www.unescap.org/tid/publication/chap3g_2160.pdf

29 Turkmenistan does not publish separate volume and price data on oil exports. However, the average world market price for crude oil was 19 per cent higher in 1996 than in 1995, and prices of oil products increased similarly. This would indicate a considerable drop in Turkmenistan's oil export volumes, or contrary to world market developments, a sharp drop in average export prices.

Turkmenistan exported electricity to the value of US$ 54 million, almost 60 per cent more than in the same period of the previous year. However, it received payments for only 43 per cent of this amount. Due to the poor payments record, Turkmenistan has stopped all electricity exports since the summer of 1996. (Table 10) offers the most recent import and export data available for 1998.Other exports amounted to US$ 77 million in 1996, 11 per cent less than in 1995. The items included in this category are, for the most part, energy-based products (white spirits, fertilizers), cotton-based products (cottonseeds), and carpets. Much of these goods are exported to other CIS countries and the decline partly reflects the changing trade patterns of these countries. After an initial surge in exports to countries outside the former Soviet Union after independence, Turkmenistan was forced back to its old markets following Gazprom's refusal to allow gas to transit the Russian Federation on the way to Europe. The CIS accounted for 59 per cent of total exports in 1997, from 68 per cent in 1996. Similarly, 50 per cent of 1997 imports came from the CIS, up from 35 per cent in 1996. Erratic items such as aircraft imports caused imports from the United States of America to rise from just $ 14 m in 1995 to a peak of $ 395 m in 1996, before dropping back to $ 88 m in 1997.

Imports

According to official data capital goods have traditionally comprised the largest component of imports. Machinery and equipment accounted for 29 per cent of total import expenditure in 1992-1997, with chemicals, metal structures and raw materials accounting for 22 per cent. Foodstuffs accounted for around 22 per cent of recorded import costs as well, and non-food consumer goods made up 15 per cent over the same period. Since the end of 1998 the Government has severely restricted imports by banning conversion of the manat, except in the case of priority state-controlled imports. In 1997 just over one-third of import costs were paid in cash, the rest being paid in barter.

Table 10: Key exports and imports, 1998

($ m unless otherwise indicated)

Exports`	**593.9**
Of which:	
Refined oil products´	243.5
Gas	70.5
Cotton Fiber	120.0
Imports	**980.7**
Of which:	
Machinery	274.6
Ferrous metals products	98.1
Electrical equipment	83.4
Vehicles	63.7
Trade balance	**-386.8**
per cent of GDP	-18.3
Memorandum items	
Export value (per cent change, year on year)	-21.0
Import value (per cent change, year on year) Real exchange rate b (official rate; per cent change, year on year) Real exchange rate b (black-market rate; per cent change, year on year)	-20.1 4.8 -29.3
Share in world exports (per cent)	0.01
Exports per head ($)	125.0

Sources: Reuters, Turkmenistan State Statistical Committee.
a EIU estimates b Year-end

FOREIGN TRADE REGIME

Foreign exchange controls affecting trade

In the past, foreign companies doing business in Turkmenistan had difficulty converting the national currency into hard currency. Some companies could not even receive manat coverage for a transaction made in Turkmenistan because of a shortage of both local and hard currency. Therefore, most trade transactions in the past were made on a barter basis (usually, payments were made in cotton). Now, the Cabinet of Ministers controls all barter transactions. In 1997, the foreign exchange rate became single and unified at 5,300 manat against the dollar and was stable until July 1998. At that time, a gap began to develop between the official rate and the black market rate, which peaked at 19,000 manat per dollar in April 1999 and has been fluctuating between 14,000 and 15,000 manat in July 2000. This has in essence resulted in an unofficial dual exchange rate that is in place today. All domestic trade is done in manat. Foreign companies may convert the manat into hard currency through their commercial banks. There are certain criteria that are taken into consideration when the SBT provides foreign exchange through its Inter bank Currency Exchange to meet the commercial banks' needs in hard currency.

Conversion and transfer policies

The Foreign Exchange Regulation Law determines general principles of foreign exchange operations, the authority of state bodies in foreign exchange regulation, and the rights of residents and non-residents regarding foreign exchange ownership and usage. According to this law, non-residents may freely convert the national currency, the manat, to hard currency without limitations or unreasonable delays, provided the amount is needed to pay for transactions made with Turkmen residents. The law also permits non-residents to repatriate capital goods previously imported into Turkmenistan, provided such goods were declared to customs upon entry. In practice, however, due to the shortage of hard currency the Central Bank provides commercial banks with limited amounts of foreign exchange to convert cash and non-cash manat sums. Not all requests for manat convertibility are serviced timely and in full amounts. That results in delays in receiving hard currency incomes and impedes doing business. A company may apply to a commercial bank to cover the amount of money to be converted with the following documents:

- An application indicating the amount of hard currency to be purchase

- A trade contract where payment terms envisage either payment for actual shipment of goods or letter of credit (contracts where prepayment Terms are envisaged are not considered);
- A customs declaration confirming cargo availability;
- A banking document confirming currency availability in either local Or foreign bank accounts;
- The commercial banks licensed to deal in hard currency submit their
- Applications for money convertibility to the Inter bank Foreign Exchange (IFE). A Presidential Decree issued on 3 December 1998 has stopped free currency exchange and approved a temporary provision limiting hard currency exchange operations. The provision provides rules and regulations concerning cash and non cash hard currency exchange for individuals and legal entities in Turkmenistan. According to the provision, only three categories of Turkmen citizens are eligible to exchange manats into hard currency in cash at the official exchange rate in commercial banks. The Central Bank[30] allows commercial banks to sell non-cash foreign exchange at the official exchange rate to legal entities that are resident in Turkmenistan only for the following purposes:
- To pay off foreign credits extended to Turkmenistan under the Turkmen
- Government sovereign guarantee;
- To repatriate foreign investments and profits providing an investment Projects registered with the State Foreign Investment Agency (SAFI) And the Chief State Tax Inspectorate (CSTI);

[30] These categories are: (1) sick people who need clinical treatment outside of Turkmenistan providing a person is enrolled in a list made by the expert commission of the Ministry of Healthcare and Medical Industry; (2) students who study abroad providing the Education Ministry confirms their enrollment; and (3) state employees who go abroad for a business trip providing a letter from an appropriate ministry or State organization approved by an appropriate Deputy Chairman of the Cabinet of Ministers is provided. For the rest of the population, the grey market is the only option for hard currency.

- To purchase medicines and medical items that are listed in a list approved by the Cabinet of Ministers;
- To purchase raw materials and other products needed for production of goods and services;
- To pay off debts on foreign credits for the promotion of private goods and services production in Turkmenistan and for the purchase of raw materials, products and spare parts needed for projects that are implemented under these credit lines; and
- To purchase consumer goods and food products (except for spirits, alcohol and tobacco) by special-purpose shops provided an obligatory contract on daily sales proceeds transfer is signed between these shops and commercial banks.

Customs regulations

Foreign companies doing business in Turkmenistan consider the Turkmen customs clearance process very complicated, in terms of paper work, and lengthy (sometimes up to 2 months). Requests for bribes have been a typical occurrence in day-to-day customs operations. To pass through customs, an importer of goods must submit the following documents[31]:

- A trade contract registered with the SCRME. The contract should contain information about quantities and costs in hard currency that will be the basis for the customs valuation;
- A bill of lading with similar information on qualities and costs;
- A customs cargo declaration form that can be obtained in the Ashgabat-Expertise firm of the Chamber of Commerce of Turkmenistan;
- A conformance certificate confirming the quality of delivered goods. The certificate can be obtained from the State Standards Inspectorate;
- A certificate of origin;

[31] http://www.unescap.org/tid/publication/chap3g_2160.pdf

- A Central Bank document confirming money transfer for purchasing goods or an irrevocable Letter of Credit.

The customs cargo declaration and bill of lading are only accepted in English or Russian. Other documents can be in Russian. The Chamber of Commerce must certify translated copies. The fee for certification ranges from USD 1 to 2 per page. Faxes and copies are not accepted as official documents by the customs authority. During the customs clearance process, Customs charges a service fee of 0.2 per cent of the contract cost and 20 per cent of the value added tax assessed on the customs service fee sum.

Tariff rates, taxes and surcharges

In 1996, the Government introduced customs excises for four categories of goods including alcohol, vehicles, tobacco products, and jewelry made of precious and semi-precious stones and medals. Gradually, the list of goods subject to customs excises has grown to more than one hundred categories of goods. The Government officially claims that there are no customs tariffs charged for export/import of goods by juridical entities. However, Turkmen Customs does, in fact, charge customs excises for export/import transactions in accordance with presidential decrees regulating export/import operations. A presidential decree of 18 August 1999 approved the updated list of goods subject to excise taxes. This list came into effect on 1 October 1999[32]. On 19 March 1999, a presidential decree introduced a 5 per cent customs duty for goods imported into Turkmenistan by individuals. The duty is charged against values determined by Turkmen Customs on the basis of world and domestic price information provided quarterly by the State Institute for Statistics and Prognosis.

Duties are not charged on goods that have been exported previously from Turkmenistan, declared at Customs and re-imported into the country. Custom also does not charge duty on goods imported as part of passenger personal luggage

[32] http://www.unescap.org/tid/publication/chap3g_2160.pdf

though the total value of goods included in the passenger personal luggage should not exceed an amount determined by Customs. Food items except for alcohol and tobacco products and medical items, school appliances and children's goods are not subject to the customs duties. Turkmen Customs levies excises on a limited number of exported goods when considering importing or exporting goods from Turkmenistan, the following should be noted[33]:

- Goods and products imported in accordance with intergovernmental agreements, governmental decrees and orders, and for implementation of projects and contracts, including those involving foreign investment, state loans, humanitarian assistance and/or raw materials that are reworked or to which value is added in Turkmenistan, are exempt from excises;
- The importation of alcohol into Turkmenistan is licensed by the Ministry of Trade and Foreign Economic Relations;

Table 11: Export Excise in Turkmenistan by Product Category

Product Category	Excise amount (US$)
(1) Pure wool and partial wool yarn	100 per ton
(2) Cattle leather:	
– leather from cows, camels, bulls, etc.	100 per ton
– leather from sheep and goats	0.50 per piece
– non-standard leather	50 per ton
(3) Ammonia saltpeter*	100 per ton
(4) Superphosphate*	100 per ton
(5) Ammonium phosphate*	100 per ton
(6) Ammonium sulphate*	100 per ton
(7) Turkmen sheep-dogs (license required from the Nature Protection Ministry)	300 per dog

Source: Ministry of Trade and Foreign Economic Relations.
Note:
* All marked products are exempt from excises when sold for hard currency through the State Commodity and Raw Exchange.
* Excises are paid in the national currency, the manat, at a foreign exchange rate determined by the Central Bank of Turkmenistan on the date of contract registration with the State Commodity and Raw Materials Exchange.

[33] ibid

OBSTACLES TO WTO MEMBERSHIP

The main obstacles to Turkmenistan's admission to WTO may be organized into geographic, economic and political categories. While some of the obstacles are structural in nature and thus difficult to remove without adequate outside help, other obstacles are merely policy-oriented and could easily be altered if the government of Turkmenistan exercises its political will to pave the way for the republic's eventual admission to WTO.

(a) Geographic obstacles

As a landlocked nation Turkmenistan's economic progress and commercial interaction with the outside world are intimately tied to its relations with the neighboring countries. Lack of access to international waters will continue to hamper Turkmenistan's incorporation into the global commercial structures. Turkmenistan has so far been heavily dependent on the Russian Federation for access to global markets. Unfortunately, the Russian Federation has been less than forthcoming in granting Turkmenistan free and unlimited access to market its products. Turkmenistan's second logical access to the world markets is through its southern neighbor, the Islamic Republic of Iran. But the United States has consistently lobbied against the Islamic Republic of Iran as an alternative transit route for Turkmenistan and other countries of the region. Although with the opening of the Sarakhs-Tajan railroad in 1996, some of Turkmenistan's commercial needs are being addressed, attempts to use or to build export pipelines through the Islamic Republic of Iran have been blocked by the United States. Finally, Turkmenistan's relations with Azerbaijan and Uzbekistan have not improved significantly over the last few years, making it difficult to use either country as a viable transit route. It is precisely this geographic predicament that makes Turkmenistan's bid for greater commercial interaction with rest of the world a difficult one, particularly in light of the that neither the Russian Federation, nor Azerbaijan or Uzbekistan are members of the WTO.

(b) Economic obstacles

Three economic obstacles will continue to weaken the prospect of Turkmenistan's admission to the WTO. First, a significant portion of Turkmenistan's trade consists of barter trade. The general lack of hard currency and the inability of trading partners to pay cash for Turkmen products make it difficult to improve Turkmenistan's commercial status as a viable candidate for admission to the WTO. This, combined with its geographic predicament, has prevented Turkmenistan from diversifying its trading partners so as to receive cash for its products. Turkmenistan's commercial interaction has remained predominantly within the old Soviet trade structure. Unfortunately, the progress to diversify its trading partners will be primarily determined by the willingness of the Russian Federation to loosen its economic grip on Turkmenistan.

Second, Turkmenistan's monetary policy will continue to be a major obstacle to the overall incorporation of its economy into the global financial structures. The adoption of a dual exchange rate has weakened Turkmenistan's competitiveness vis-à-vis its trading partners. (Table 12) provides a clear picture of the impact. The table demonstrates the unweighted real exchange rate of manat vis-à-vis the currencies of the trading partners and a sample of semi-industrialized countries. The real exchange rate appreciated significantly against the currencies of the all partners during the 1995-1999 periods. Of particular significance is the deterioration of Turkmenistan's competitiveness in the markets of its actual and potential trading partners, including Czech Republic, Poland, Turkey and Ukraine.

Furthermore, given the appreciation of the Turkmen manat against all other currencies in the sample, Turkmen products face a steep competition in the Russian, Ukrainian, and Eastern European markets from competitor countries[34].

Finally, given the structure of the Turkmen economy, which is largely dependent upon gas and cotton, the country will continue to face a rather limited

[34] http://www.unescap.org/tid/publication/chap3g_2160.pdf

trade capacity. The hard currency shortages and barter trade have severely hampered the government's ability to diversify the economy. This trend will most likely continue in the near future, unless Turkmenistan is given access to markets that

Provide hard currency for its export trade[35].

Table 12: Real Exchange Rate Index, 1995-1999

	1995	1996	1997	1998	1999	
	Year	Q4	Q4	Q3	Q1	Q4
Turkmenistan/Armenia	100	193	231	262	316	347
Turkmenistan/Azerbaijan	100	172	200	216	290	361
Turkmenistan/Belarus	100	193	278	336	565	475
Turkmenistan/Estonia	100	184	236	246	290	342
Turkmenistan/Georgia	100	172	207	239	387	380
Turkmenistan/Kazakhstan	100	177	212	230	307	475
Turkmenistan/Kyrgyzstan	100	217	256	302	481	584
Turkmenistan/Lithuania	100	173	200	212	255	284
Turkmenistan/Latvia	100	184	227	246	285	311
Turkmenistan/Moldova	100	174	199	221	387	441
Turkmenistan/Russian Federation	100	193	235	326	576	606
Turkmenistan/Tajikistan	100	243	274	322	440	544
Turkmenistan/Ukraine	100	172	201	264	406	528
Turkmenistan/Uzbekistan	100	213	265	326	362	431

Source: International Monetary Fund, "The Burden of Current Agricultural Policies", Working Paper, June 2000, WP/00/98. An increase to the index indicates an appreciation of the manat vis-à-vis the currency of Turkmenistan's trading partner.

(c) Political obstacles

From a political point of view, Turkmenistan has been faced with sérious obstacles. First, in an attempt to keep Turkmenistan within its sphere of influence the Russian Federation has consistently forced Turkmenistan to abide by terms and conditions unfavorable to its export trade. The Russian Federation has a virtual monopoly over gas export pipelines and to a large extent controls the

[35] ibid

Turkmen gas export destinations[36]. Two aspects of Russian policy have been particularly detrimental to the Turkmen economy. First, due to lack of alternative pipeline access, Turkmenistan has been forced to sell its gas at way below global market prices. Second, Russian pressure has so far prevented Turkmenistan to export to European markets directly and in large quantities so as to earn greater amounts of hard currency. The second obstacle has to do with the nature of political rule in Turkmenistan. President Saparmurat Niyazov has so far resisted meaningful structural reforms and continues to pursue a policy of state-led economic system. In the absence of any significant structural reform, the state will continue to retain tight control over the key sectors of the economy and over access to imports, credit, and foreign currency. Furthermore, to prevent further deterioration of living standards, Mr. Niyazov has continued subsidizing virtually all daily necessities from gas to electricity to bread at a high cost and at the expense of meaningful domestic investment in the economy. An inevitable by-product of Mr. Niyazov's policy of control has been a very slow growth of independent entrepreneurship and commercial activities[37].

TAJIKISTAN

The Republic of Tajikistan started the process of radical social-economic reforms, restructuring of the political system and establishment of a democratic and secular state in 1991 as an independent state[38]. Unfortunately, as a result of the break-down of existing interstate relations within the former Soviet Union the country witnessed a long-term macro-economic and socio-political crisis in the country. The situation was deteriorated by natural disasters and most of all, civil conflict, which contributed to the destruction of the national economy. Stability was restored only in 1997 with the signing of a peace agreement between the

36 http://www.unescap.org/tid/publication/chap3g_2160.pdf

37 ibid

38 http://www.unescap.org/tid/publication/chap3f_2160.pdf

Government of Tajikistan and the United Tajik opposition and a new coalition government was established[39]. The peace and reconciliation process, supported by the international community, has progressed well since then and has facilitated the rehabilitation of the national economy and rendered economic growth. Between 1991-1997, the level of GDP diminished by more than 60 per cent which significantly reduced the living standards of the less protected part of the population. The GDP per capita rate of Tajikistan is one of the lowest among CIS countries. The average salary rate still remains low in Tajikistan. Much of the country's production infrastructure is in urgent need of repair and restoration after years of war damage and due to the lack of proper maintenance[40].

Tajikistan is an agrarian country. Almost half of the labour force is employed, in the agricultural sector while more than 70 per cent of the total population lives in rural areas. A favorable bio-climate condition renders opportunities for the Tajikistan[41] significant development of this sector.

In particular, Tajikistan has great potential for cotton growing. In line with the President's program of reforming the agricultural sector, 75 thousands hectares of land-plots were distributed among the rural population. In 2000, 10,800 farm enterprises operated in Tajikistan. This allowed an increase of the value of grain production up to 600,000 metric tons per year. However, it should be emphasized that the agricultural sector of the economy is in a difficult situation because of the absence of adequate equipment and technology and an undeveloped infrastructure. The industrial sector witnessed an uneven development and is dominated by a few sub-sectors, such as metallurgy and light industry. The largest industrial plant is the huge aluminum smelter (TadAZ), with annual installed output capacity of

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39 ibid

40 ibid

41 Based on a paper prepared by Mr. Negmatullo Inoyatov, Head and Department of Relations with non-CIS Countries, Ministry of Economy and Trade, Tajikistan. *Country papers on accession to the WTO* 253 available at :

more than 550,000 tons of aluminum. There is no adequately developed mining and chemical industry, though these sub-sectors have great potential[42].

The country prospected more than 400 deposits of mineral sources and has big deposits of gas and fuel. Tajikistan also has large capacity for the production of hydro-electricity power (more than 400bln. kV) and disposes of large water resources[43].

During 1998-2000 almost all sectors of the national economy witnessed output growth. According to official statistical data for 2000, GDP growth was 8.3 per cent. Industry accounted for 20.5 per cent of GDP in 2000, agriculture 17 per cent, and services 39.1 per cent[44].

FOREIGN TRADE STRUCTURE

After independence the direction of foreign trade of Tajikistan changed significantly. At the beginning of the 1990s about 85 per cent of the country's foreign trade was with countries of the former Soviet Union. With the rupture of traditional trade and economic links within the former Soviet Union System and the collapse of the payment system Tajikistan was forced to seek for new markets.

Preference was given to Western European countries, where the biggest aluminum and cotton exchanges are located. As a result, the share of non-CIS countries in Tajikistan's foreign trade turnover increased to a level of 50-70 per cent in 1994-1997. Among the main trading partners of Tajikistan are Belgium, Germany, Italy, Liechtenstein, Netherlands, Switzerland and the United Kingdom. The main exports to these countries are raw cotton and aluminum. Since 1998 Tajikistan has restored trade-economic links with its traditional partners in the CIS and share of these countries in Tajikistan's foreign trade increased to a level of 55-60 per cent (table 13).The analysis shows that the commodity structure of foreign

[42] http://www.unescap.org/tid/publication/chap3f_2160.pdf

[43] ibid

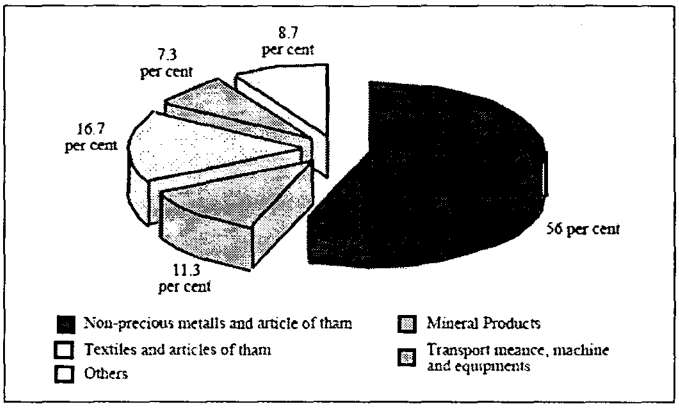
[44] ibid

trade is very straightforward. The undesirable foreign trade structure of Tajikistan is dominated by export of raw materials and import of food stuff and energy sources. At present the Government of Tajikistan has taken some measures to stimulate domestic producers to develop import substitution industries (figures 1and 2)[45].

Table 13: Foreign Trade Turnover of Tajikistan during the period of 1996-2000 (US$ m)

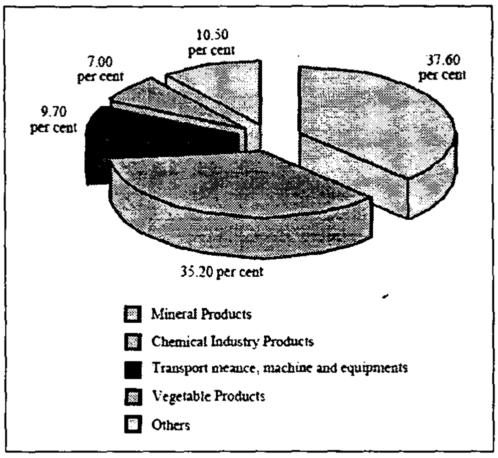
	1996	1997	1998	1999	2000
Foreign Trade of Tajikistan, total	1 438.2	1 581.2	1 307.6	1 455.7	1 453.4
Including:					
CIS countries	713.5	813.4	785.5	797.1	927.6
Non CIS countries	724.7	767.8	522.1	658.6	525.8
Export from Tajikistan	770.1	784.7	596.7	688.7	779.1
Including:					
CIS countries	331.0	310.9	223.0	281.6	368.6
Non CIS countries	439.1	473.7	373.7	393.8	410.5
Import to Tajikistan	668.1	796.6	711.0	663.8	674.3
Including:					
CIS countries	382.5	502.5	562.6	515.5	559.0
Non-CIS countries	285.6	294.1	148.4	264.8	115.3

Figure 1: Commodity structure of Tajikistan Exports



45 ibid

Figure 2: Commodity structure of Tajikistan Exports



FOREIGN TRADE REGIME

Trade and investment policies

In 1998 the Government of Tajikistan in collaboration with the IMF adopted a new medium-term program of economic reform for the period of 1998-2001, which aims to achieve macro-economic stability in the country. The key targets of the Program are: (a) maintenance of economic growth at a level of 6 per cent during whole period of Program implementation, (b) reduction of the budget deficit up to 1.6 per cent of GDP in 2001, and (c) reduce annual inflation to a level of 13 per cent[46].

Significant success was achieved in the implementation of structural reform policies. Following privatization of the small enterprises, attention will be given to privatization of large-scale enterprises. In 2001, the Government intends to privatize in addition 130 entities and increase the implementation of large-scale enterprise privatization up to 40 per cent.

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46 ibid

Promotion of Foreign Direct Investment

Since independence the legislative and regulatory framework for the establishment of a market-oriented economy in the country has been developed[47]. The Law on Privatization of State-Owned Property encourages the participation of foreign investors in the privatization of the national economy[48]. Within the context of bilateral relations the Government of Tajikistan signed agreements on promotion and mutual protection of investments with a number of countries, which form the basis for the regulatory framework for investment activity in Tajikistan. At present, more than 210 joint ventures are established in Tajikistan. The main areas of activities of joint ventures are textiles, output of necessary products, export-import operations, agro-processing, construction and construction materials, telecommunications, and mineral resources exploration[49]. Big enterprises, such as Tajik-British "Zarafshon" and "Darvoz" in the field of gold exploration, Tajik-Korean "Tajik-Cabool-Textiles", Tajik-American "Khujand" and Tajik-Italian "Javony" in the field of cotton processing are already operating in Tajikistan. In line with objectives of the Government, the investment program for 1999-2001 targets foreign direct investment for construction of a water-energy station, exploration and processing of mineral resources, cotton-processing and export of textiles, production and export of citrus, processing of cattle breeding products and production of final goods, increasing of output of fertilizers, production of consumer goods, reconstruction and modernization of existing agricultural capacities, creation of progressive and scientific industrial sub-sectors, and development of the telecommunications system. With regard to the external economic sector, the Government of Tajikistan has implemented reforms since independence. The main principles and rules of the external economic activities in Tajikistan are determined by the Law on Foreign Economic Activities of

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47 ibid

48 ibid

49 ibid

Tajikistan, adopted in 1993. This document creates the basis for activities of all foreign economic subjects in a country, protects their rights, interest and properties in accordance with accepted standards of international law on a fair and equal basis and strengthens integration of the national economy into the world economy[50].

Another important legislative act regulating external economic activity is the Law on Foreign investment, adopted in 1992 (amendments and additional remarks made in 1996, 1997 and 1999). This law, which creates a quite favorable investment climate for foreign investors, secures the rights and interests of foreign investors and economic subjects[51].

Trade Liberalization

The adoption of the two legislative acts mentioned above in the early stage of reform allowed the strengthening of trade-economic relations of Tajikistan with the rest of the world. But economic reforms have progressed well since 1995 after the adoption of the resolutions on Foreign Trade Liberalization in the Republic of Tajikistan on 27 June 1995 and on Liberalization of Currency and Export Operation on 24 February 1996. Administrative constraints and trade protective measures have been gradually removed. Since 1 February 1996 the quota and licensing system in a country have been eliminated. Later, in February 1997, the obligatory examination of import-export contracts was also abolished. At present Tajikistan's foreign trade policy is oriented towards development of the export potential of the country. Tajikistan has an undesirable trade structure: the main share of export is made up by raw materials, while inefficient imports are dominated by foodstuffs and energy-products[52].

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50 ibid

51 ibid

52 ibid

The Government has applied a progressive approach to trade liberalization. Initially, liberalization covered practically all export categories, except a few items, including cotton and aluminum. During the second stage, 1996-1997, the Government gradually liberalized trade in the two main export items: cotton and aluminum and established necessary financial institutions, such as the Cotton-Exchange, and the Tajik Universal Commodity and Raw Material Exchange. All these measures allowed an increase of the export potential of the country and stimulated foreign trade. As a result, since 1996 Tajikistan has maintained a positive trade balance, to some extent, has led to the normalization of currency transactions and balance of payments stabilization.

During 1995-1997, 100 per cent pre-payment mechanisms for a limited range of export categories (ten items) were introduced. For other exports payment periods were limited from 90 up to 120 financial days. These measures were reluctantly introduced in order to develop a proper mechanism for currency transactions.

In order to stimulate exports and promote foreign trade the Government of Tajikistan adopted an export promotion policy. Export duties were abolished and differential rates for import duties were adopted. It should be pointed out that the accepted rates of import duties are generally lower than those in neighboring countries, except Kyrgyzstan.

Since independence, Tajikistan has created trade-economic links with more than 80 countries all over the world. These trade-economic relations are developed on the basis of bilateral agreement and treaties on trade-economic co-operation, which routinely include a clause on most-favored nation (MFN) treatment. At the same time, Tajikistan pays attention to the development of relations within the framework of regional trading arrangements and custom unions. Today Tajikistan is a member of the Euro-Asian Economic Community, CIS, Central-Asian Economic Community, ECO and so one. Membership in such arrangements and organizations provide opportunities to the country to benefit from privileges granted by all member countries[53].

Current trade regime

With the purpose to implement the Treaty on strengthening integratión and regional cooperation in the economic and humanitarian fields among Belarus, the Russian Federation, Kazakhstan and Kyrgyzstan, dated 29 March 1996, and taking into consideration the fact that Tajikistan joined the Agreements establishing the Customs Union, dated 20 January 1995, the Government introduced a new tariff regime by Resolution no.1 dated 7 January 1999.

In accordance with this resolution, zero import tariffs were introduced for products originating from Customs Union Member countries. Also, a preferential regime and fixed zero tariff rates with respect to the least developed countries were introduced. On average, tariff rates in Tajikistan vary from 5 up to 30 per cent, depending on the import item. As mentioned before, there are no export and import non-tariff barriers in Tajikistan. Exceptions are exports and imports which have an impact on state security of the country, such as defense, health care, cultural artifacts and antiques and so one. The Government also controls the export and import of electricity and natural gas.

PREPARATIONS FOR ACCESSION TO WTO

In according with the priorities of the Government of Tajikistan, declared in program documents and resolutions, the country aims to deepen the integration of its national economy into the world economy. In this context, one of the key issues of the external economic policy of Tajikistan for the nearest future will be accession to the WTO. It is well known that the WTO is the legal and institutional foundation of the multilateral trading system. Most nations, including almost all the main trading nations, are members of this system. The system's overriding

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[53] ibid

purpose is to help trade flow as freely and fairly as possible, as long as there are no undesirable side effects. Under the WTO Agreements, countries cannot normally discriminate among their trading partners. This point is very important for the young and sovereign nation of Tajikistan, which is on its way to establish a democratic and secular state and market-oriented economy.

However, it cannot be denied that the accession process is a long and laborious process. It requires adoption of a lot of legislative acts, so as to conform the national legal framework to the rules and regulations of WTO; and involves comprehensive and intensive negotiations with all WTO members concerning trade regimes, tariff and non-tariff measures, eliminating barriers in international trade and so on.

As mentioned before, the Government of Tajikistan has already established a rather developed legal framework which would meet world standards. The trade regime in the country is currently sufficiently liberalized. Tariff and non-tariff barriers have been reduced to a minimum. By Government Decision no. 10-r dated 4 February 1999, a Working Group – the Interdepartmental Commission on WTO Accession Material Preparation, headed by the Deputy Minister of Economy and Trade of Tajikistan, was established.

This Working Group maintains close contacts with UNITAR, and the SECO Secretariat (the Swiss State Secretariat for Economic Affairs and Coördination Office for Issues related to WTO Accession). A series of seminars and workshops jointly organized with UNITAR in Dushanbe during 1999-2001 attracted high level officials from government bodies, members of the Working Group, and parliamentarians.

The main issue for Tajikistan during the accession process will be TRIPS. Tajikistan has a National Patent and Information Center within the Ministry of Economy and Trade. Among the main responsibilities of this Center is the protection of state interests in the areas of invention, industrial samples, trade mark and service marks. Tajikistan is represented in the International Union for the Protection of New Varieties of Plants (UPOV) and is the member of the Euro-Asian patent convention. Also, Tajikistan has taken measures to implement the stipulations of the TRIPs Agreement related to protection of copy (author's) rights. At present, within the Ministry of culture of Tajikistan, there is an agency for copyrights. Tajikistan is a member of the World Convention on Copyrights, and since March 2000 – a member of the Bern Convention on protection of works of literature and art. Tajikistan created the legislative framework in line with world standards. On 13 November, 1998 the country adopted the Law on Copyrights, which passed an examination of WIPO and protects authors' rights in accordance with the international conventions. These facilities and arrangements lay the basis for an accelerated accession of Tajikistan to WTO. Tajikistan formally applied for WTO membership in May 2001. Unfortunately, Tajikistan is among the last among the CIS countries to have formally submitted its application. According to the requests of the Tajikistan delegation to the WTO General Council, Tajikistan's application will be considered at the next WTO General Council Meeting on 18 July 2001[54].

With reference to integration of Tajikistan into the Multilateral Trading System and, particularly, the accession of the country to the WTO, it should be pointed out that Tajikistan as a country with a relatively small economy and limited possibilities for international trade will not have a major impact on international trading conditions. In this respect, accession to the multilateral trading systems is vital for the country as it would accord the country protection from discriminatory trade practices of the main trading nations and most favored nation treatments under the various WTO Agreements.

Accession to the WTO would have the following advantages for the country:

- To benefit from MFN treatment under the various WTO Agreements;

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[54] ibid

- To benefit from the world-wide free trade rules-based system, including the elimination of restrictive trade barriers and discrimination measures applied to the country in international trade;
- To have access to the international trade information systems, which allow an in-depth analysis of world market structures and conditions and formulation of effective trade and economic policies.
- To have opportunities to consult with WTO Member Countries so as to develop new trade partners and new markets;
- Within the framework of WTO it would be possible to train highly qualified specialists in the areas of international trade and external economic relations;
- Finally, accession to the WTO would allow the country to strengthen its reputation and image in the world and will create favorable conditions for the attraction of foreign investment to the country. At the same time, it is essential that the country is well aware of the obligations and commitments it will assume as a WTO member. It will be a challenge to balance Tajikistan's internal interests with meeting WTO Member Countries' demands and to apply a correct approach to the accession process which would protect it from potentially negative consequences as a result of a too hurried accession process.

KYRGYGSTAN

Since independence from the Soviet Union in 1991, the Kyrgyz Republic has undertaken an ambitious program of economic reforms[55]. These reforms have considerably reduced the role of the government in the economy by introducing market forces. Mass privatization and price liberalization have been pursued, so as to establish a liberal trade and investment environment open to international

[55] This section is based on *"Kyrgyz Republic: Selected Issues and Statistical Appendix"*, IMF Staff Country Report, October 2000.

exchanges[56]. In 1998, after a referendum, full private ownership of land was allowed; the Kyrgyz Republic was the first country in the Commonwealth of Independent States (CIS) to introduce such a measure. Despite these reforms, recent developments, including those resulting from the financial crisis in Russia, have shown the economy to be less robust than expected. As in all the other countries of the former Soviet Union, output declined in the Kyrgyz Republic over the initial period of transition and didn't recover until 1996. Recovery was largely driven by the start-up of production of the Kumtor gold mine and over the next two years, real GDP growth expanded by around 7-10 % per annum[57]. This favorable performance came to an abrupt halt, however, in the second half of 1998, with the Russian financial crisis. Therefore, the economy remains vulnerable to external shocks since macroeconomic stability has not been achieved yet. In 2000 GDP amounted to 1.3 billion US$[58] (thus recovering if compared to the previous year). Agriculture continues to drive the economy, accounting for around 40% of GDP: this makes growth strongly dependent on favorable weather conditions. Nevertheless, industry also plays an important role in Kyrgyz economy, accounting for 21,3% of GDP, most of which is attributable to gold mining. The services sector accounts for over 30% of GDP.

FOREIGN TRADE STRUCTURE

As far as trade is concerned, the Kyrgyz Republic is a small but open economy. It was the first country among those of the former Soviet Union to enter the WTO in 1998. Exports are mainly based on agriculture, electricity, water and, above all, gold. Actually, gold accounts for more than 80% of exports to non-CIS markets, especially to Germany[59] .Apart from Kumtor production, the Kyrgyz

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56 http://www.intracen.org/worldtradenet/docs/networking/country_papers/paper_kyrkyzstan.pdf.

57 http://www.intracen.org/worldtradenet/docs/networking/country_papers/paper_kyrkyzstan.pdf.

58 The Economist Intelligence Unit, Country Report, July 2001

59 Exports to Germany alone accounted for almost 45% of total export revenue in the first quarter of 2001 (see: EIU, Country Report, July 2001).

Republic possesses few other reliable export possibilities. Electricity exports, for example, depend on fluctuating Uzbek demand and export policies. This second largest export category accounted for about one-sixth of total exports in 2000. Imports mainly consist of machinery and energy. In the first quarter of 2001, there was a further decline in import expenditure, following the trend of last years. This has resulted in a reduction of the trade and the current-account deficit, but it has raised other concerns. In fact, machinery and energy inputs are essential to guarantee recovery in the nongold industrial sector.

Main economic indicators, [60]

- Population: 5,004,000
- Total area: 198,500 sq. km
- GDP: $2.1 billion
- GDP growth rate: –0.5%
- GDP per capita: $457
- Major exports: electricity, machinery, foodstuffs
- Exports of goods and services: $589 million
- Major export trading partners: Switzerland 20.3%, Russia 16.4%, China 8.4%, Kazakhstan 7.5%
- Major imports: machinery, oil and gas, chemicals, foodstuffs
- Imports of goods and services: $578 million
- Major import trading partners: Kazakhstan 21.1%, Russia 19.9%, Uzbekistan 10.2% China 10.1% U.S 8.1%
- Foreign direct investment (net): $4.2 million

[60] available at www.heritage.org/research/ features /index/country files/Kyrgyz republic

Table 14: Trade In Goods And Services

Foreign trade, 2000 US$m	
Export of goods	***504.5***
Agriculture	46.9
Manufacturing	457.5
Of which:	
non-ferrous metallurgy	234.4
electricity	79.8
machine-building	53.7
light industry	43.9
Imports of goods (cif)	***554.1***
Agriculture	40.9
Manufacturing	513.2
Of which:	
Machine-building	150.6
Oil and gas	120.8
Food industry	46.9
Light industry	38.8
Trade balance	**-49.6**

Source: Kyrgyz National Statistical Committee[61].

After the dissolution of the Soviet Union, the Kyrgyz Republic engaged in rapid trade liberalization and is now one of the most open economies among the Baltics, Russia and other countries of the former Soviet Union. In December 1998 it became the first of these countries to join the World Trade Organization (WTO). Nevertheless, efforts to diversify its trading partners, as well as export goods, have not been easy. The Kyrgyz Republic's geographical isolation and dependence on fuel imports has left it highly dependent on imports from the other members of the CIS. Expenditure on imports from the CIS as a percentage of total import costs has therefore fallen only moderately, averaging about 50% in 1998-2000, compared with just over 60% in 1994- 97. Russia remains the largest source of imports, accounting for 20-25% of total imports, and Uzbekistan and Kazakhstan are also important sources, accounting for 14% and 10%, respectively, of import

61 http://www.intracen.org/worldtradenet/docs/networking/country_papers/paper_kyrkyzstan.pdf.

expenditure in 2000. The Kyrgyz Republic has been more successful in diversifying its export markets, although this is almost solely a function of the start of gold production at the Kumtor mine in 1997, and has come at the cost of over-reliance on a single export commodity. As a result of Kumtor production, the gold sector's share of total export revenue rose from around 15% in 1994-95 to about 50% in 1999-2000. As industrialized Western countries provide the principal markets for Kyrgyz gold exports, export revenue from markets in the CIS fell from an average of almost 70% in the mid-1990s to just above 40% by the end of the decade. Germany became by far the largest export market in 1998, when its share of total exports jumped from 3% to 37%. Since sales of gold accounts for about 80% of all non-CIS exports, the country remains extremely vulnerable to fluctuations in world gold prices, which have fallen by more than 20% since the start of Kumtor production in 1997, and are not expected to recover quickly. The Kyrgyz Republic has recorded a sharp decline in trade turnover since mid- 1990s, with both export revenue and import expenditure in 2000 down by around one-fifth from 1997 levels. On the import side, this reflects both the effects of the Russian crisis and the great expenditure on machinery and equipment for the construction of the Kumtor mine. With export revenue rising at far slower rate, the trade deficit increased sharply to around 14% of GDP in 1996, up from 8% of GDP in 1995, resulting in a current-account deficit in 1996 equivalent to more than 23% of GDP. Faced with a lack of investment in the non-gold export sector, Kyrgyz exports have therefore recovered only gradually from the sharp decline experienced after the regional economics downturn in 1998. Gold export revenue has risen only moderately, with weak prices partly offsetting increased production levels, and in 2000 other leading exports, such as machinery, were still well down on 1998 levels[62].

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[62] http://www.intracen.org/worldtradenet/docs/networking/country_papers/paper_kyrkyzstan.pdf.

Table 15: Main trading partners, 2000
(% of total)

Exports fob to:	
Germany	28.7
Uzbekistan	17.7
Russia	12.2
China	8.7
Switzerland	6.8
Imports cif from:	
Russia	23.9
Uzbekistan	13.5
Kazakhstan	10.3
US	9.7
China	6.7

Source: Kyrgyz National Statistical Committee.

FOREIGN TRADE REGIME

The strategies and priorities of Kyrgyzstan's foreign trade policy are described in the "Complex Development Framework of the Kyrgyz Republic till 2010" (CDF)[63]. According to the CDF, a liberal foreign policy, greater use of advantages available from WTO membership and opportunities represented by regional cooperation will enable the country almost double export income by the year 2010. The key areas of needs and opportunities in foreign trade development can be summarized as follows:

Intra-regional trade development in central Asia

The Kyrgyz Republic[64] needs, first of all, to improve its relations with neighboring countries. In fact, since Kyrgyzstan entered the WTO, the other Central Asian countries have been imposing restrictive measures. These limitations, together with transit problems, rules of transportation of some groups

[63] This section is based on a draft report by Baktybek Rakhimov (National Consultant), August 2001, for a project of **trade** promotion of the Kyrgyz Government

[64] http://www.heritage.org/about/advancedsearch.cfm

of commodities and excise taxes on Kyrgyz goods significantly affect on volume of foreign trade. So, the Kyrgyz Republic continues negotiating with them on water, gas, electricity delivery issues, and about the elimination of trade barriers. These matters can been raised at a recently established Interstate Council of the Republic of Kazakhstan, Kyrgyzstan and Uzbekistan to address these type of issues. In any event, membership of the WTO provides Kyrgyzstan with another place where these issues can be resolved, in particular while the other two countries are seeking to entry the WTO themselves.

Development and implementation of national export development strategies

The main objective of Kyrgyz foreign trade policy is to increase the volume of exports in goods and services. Therefore, the State Program "Export-Import till 2002" emphasizes an urgent need to eliminate some factors restricting foreign trade development:

- Insufficient production output and low competitiveness of Kyrgyz export goods;
- Loss of traditional markets and lack of marketing skills for entering new markets;
- Weakly encouraging financial and tax incentives, and absence of guarantees and Export credit insurance.

It is also important for the Kyrgyz Republic to make extensive use of possibilities available within WTO, regional and bilateral **trade** and economic agreements[65].

Capacity building of SMEs regarding the Multilateral Trading System

As stated in the program, small and medium-sized enterprises play a key role in providing employment, reducing poverty, creating a competitive environment, and searching for new directions for profitable development. Therefore, the state has to create a favorable legislative and institutional

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[65] http://www.intracen.org/worldtradenet/docs/networking/country_papers/paper_kyrkyzstan.pdf

environment that maximizes the activity of this sector of the economy. Among other things, this includes:

- Informational and educational support, e.g. through the access to export databases;
- Promotion of the creation of associations of entrepreneurs;
- Creation of a system for advisory and consulting services;
- Participation in trade exhibitions/fairs abroad financed by state institutions. This strategy aims at improving competitiveness of the SME sector, against domestic and foreign enterprises, and at growing exports by the SME sector.

Public and private sector procurement

In the past years, the Kyrgyz Republic initiated a process of reforms in the public procurement system, which culminated in the adoption of the Law "On State Procurement of goods, works and services" (1997). The development of public sector procurement is supported my many donor organization.

Capacity building in quality management

Kyrgyzstan's integration into the world economic system, development of exports and mutually beneficial trade with leading countries require accelerated improvement of quality and competitiveness of goods. In fact, Kyrgyz exports should meet international standards, including packaging and labeling. In connection with its membership in the WTO, the Kyrgyz government is paying attention to reform the state system of certification, in order to implement the provisions of the Agreement on Technical Barriers to Trade (TBT) and to introduce ISO and IEC international standards

THE KYRGYZ REPUBLIC AND THE WTO

The Kyrgyz Republic applied for membership in the WTO in February 1996. In December 1998, it became the first BRO[66] country to join the WTO (Latvia and Estonia followed in 1999), thus showing its openness to the international trade system. Kyrgyz participation in the WTO has become a significant step towards integration into the international trading system and solution of existing problems of foreign trade policy[67].

In order to join the WTO, the Kyrgyz Republic was required to complete three "phases" of accession: 1- completion of a Memorandum on Foreign Trade Regime which described trade policies and institutions, 2- fact finding by the WTO members, 3- bilateral negotiations with all WTO members: each WTO member is entitled to undertake bilateral negotiations for increased market access and reductions in trade restrictions with the applicant. In this sense, the negotiations are unidirectional, because only the members make demands during the negotiations. Once the negotiation is concluded, the country is invited to join the WTO[68].

Concessions

Since the Kyrgyz Republic had a relatively open economy with few trade restrictions and a low uniform tariff, it didn't have to make many concessions to gain membership in the WTO. The primary concession that they agreed to, and which has been difficult to implement, involves collection of the VAT. Most CIS countries have adopted a mixed system of VAT collection, which is "origin" based for CIS countries and "destination" based for non-CIS countries. The "origin" principle involves payment of the VAT when the good is exported or sold domestically. Instead, the "destination" principle involves payment of the VAT

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66 BRO: Baltics, Russia and other countries from the former Soviet Union

67 http://www.intracen.org/worldtradenet/docs/networking/country_papers/paper_kyrkyzstan.pdf

68 http://www.intracen.org/worldtradenet/docs/networking/country_papers/paper_kyrkyzstan.pdf

when the good arrives at its destination, which means that imported goods require a VAT payment and exported goods are tax-free. As a requirement for WTO membership, the Kyrgyz Republic agreed to amend its tax code to apply the destination principle to all exports and imports, including those of the CIS, by January 1, 1999. In terms of goods and services concessions, the Kyrgyz seem to have made relatively few concessions on services appear to be limited to the elimination of requirements permitting only Kyrgyz citizens or firms to apply for certain licenses[69].

Market Access

By joining the WTO, the Kyrgyz Republic is automatically entitled to unconditional Most Favored Nation (MFN) status by all other WTO members. However, reductions In trade barriers are only effective if there is significant trade between the countries. Unfortunately, four of its six major trading partners are not members of the WTO. The pattern of trade that has emerged since 1995 indicates that the Kyrgyz Republic has shifted some trade away from its traditional trading partners and towards WTO members (especially towards Germany and the US). However, although trade with Kazakhstan and Russia has declined, these countries still accounts for the largest share of the Kyrgyz Republic's trade.

Benefits of WTO Membership

Generally speaking, the Kyrgyz Republic has acquired important benefits from its accession to the WTO system. Firstly, WTO membership requires that domestic policies be consistent with international practice through the development of internal institutions and a reduction of the role of government in the economy. Therefore, the participation in the multilateral trading system could provide the Kyrgyz government with better legal standards and a push toward the development of a market-based economy. Secondly, the rule-based WTO

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[69] ibid

mechanism and its dispute settlement system can be very important for small country like the Kyrgyz Republic because it lacks the political and economic strength to influence, on its own, trade issues that may affect it. However, since most of the Kyrgyz commercial partners stand outside the WTO, this mechanism holds only a limited value at the moment. This situation, however, will change with the accession of China, Russia and other countries of the region to the WTO. Moreover, the presence of the Kyrgyz Republic inside the WTO could facilitate the accession of its major trading partners: Russia, Kazakhstan and Uzbekistan, for example. More specifically, the membership of the Kyrgyz Republic in the WTO gives the country the following advantages:

- Access to new markets for exporting of Kyrgyz goods and services;
- Introduction of Most Favorite Nation regime for goods from the Kyrgyz Republic in the markets of importer countries;
- More attractive, stable and predictable conditions for investments;
- Broader assortment of better quality goods and services at lower prices for consumers of the republic;
- Access to an efficient dispute settlement mechanism;
- Bringing trade, investment and customs regulations into accord with international standards;
- Freedom of transit through territories of WTO member countries;
- Better access to world market information.

In connection with the intentions of other countries of CIS to enter to the WTO, early membership gives the Kyrgyz Republic specific advantages:

- Country promotion worldwide and competitive advantages before later joining countries;
- Rights to influence accession to the WTO in respect of newly acceding countries;
- strengthening of Kyrgyzstan's trade administration bodies;
- Right to participate in the preparation of new WTO rules.

Trade effects of WTO membership

As the table below shows, after accession to the WTO there has been a notable shift in the pattern away from central Asia and Russia towards Europe. This shift is largely due to falls in export to Kazakhstan, Uzbekistan and China. In fact, each of these countries responded to the financial crisis in Russia by restricting trade flows.

Table 16: Exports by country (% of total exports)

	1995	**1996**	**1997**	**1998**	**1999**
Europe	41%	36%	53%	65%	63%
Asia	57%	60%	44%	34%	34%
Other	1%	4%	3%	1%	3%
Central Asia					
Kazakhstan	16%	22%	14%	17%	10%
Tajikistan	2%	2%	2%	2%	2%
Turkmenistan	1%	1%	0%	0%	1%
Uzbekistan	17%	23%	17%	7%	10%
Sub Total	***36%***	***48%***	***33%***	***26%***	***23%***
China	17%	7%	5%	3%	6%
Russia	26%	27%	16%	16%	16%
Germany	1%	1%	3%	37%	33%

Source: See: Constantine Michalopoulos and David Tarr "The Economics of Customs Unions in The Commonwealth of Independent States", June 1997. This paper— a joint product of the International Trade Division, International Economics Department, and the Russia and Central Asia Department— is part of a larger effort in the World Bank to analyze the effects of different trade regimes in countries in transition.

The Experience of the Kyrgyz Republic

The Kyrgyz Republic's WTO experience has become a disputed element in trade policy debates elsewhere in Central Asia and in Azerbaijan. Opponents of WTO membership cite the Kyrgyz Republic's poor economic performance since 1998 as evidence of a harmful effect of WTO membership. Such an interpretation is difficult to prove or disprove empirically given the many other candidates for explaining the country's disappointing economic performance in the final years of the century. The 1998 Russian Crisis, Kazakhstan's large currency devaluation, and the Kyrgyz Republic's massive banking crisis (three of the country's four largest banks were liquidated in 1998 and 1999) were major negative shocks to the Kyrgyz economy which coincided with WTO accession. The weakened economy of the Kyrgyz Republic certainly failed to reap much in the way of immediate benefits from WTO membership, but it is hard to demonstrate that it suffered harm from accession[70].A more robust criticism of the Kyrgyz Republic's accession experience is that the negotiators, whether due to inexperience or by intent, failed to make transitional arrangements or gain exemptions that would have protected Kyrgyz interests. Some learning process is reflected in Kazakhstan's lengthier and more detailed WTO negotiations, and harder stance on some of the voluntary codes. The appropriate negotiating balance must reflect a country's preferences and compliance capabilities; immediate compliance may be problematic and a phasing-in period desirable. It is, however, unlikely that WTO provisions would harm a small open economy, although specific interest groups in the country may lose out. The basic WTO principles, embodied in the General Agreement on Tariffs and Trade (GATT), are general in applicability, and, although every nation has its own specific features, they do not imply that the WTO principles need to be modified. A red herring for many CIS countries (and China) in their WTO accession negotiations has been the pursuance of developing country status in order to qualify for special and differential treatment. All of the evidence suggests that developing country status has been of little value to its beneficiaries[71]. On the other hand, the CIS countries have made little effort to shed their "transition"

[70] Trend (2003, 55-60) contrasts the 7-9% GDP growth of 1996 and 1997 with the 2-5% growth in the years 1998-2001. The Azerbaijani report mentions the other negative shocks, but focuses on WTO accession as the main cause of disappointing post-1998 growth, alleviated only by exports from the Kumtor goldmine whose growth was independent of WTO status. In a study of twenty-five transition economies during the period 1990-8, Campos (2004) found no robust relationship between WTO membership and the rate of economic growth, although he did find a positive effect of WTO membership on domestic reform; see also, Bachetta and Drabek (2002).

[71] Donor-determined schemes under the Generalized System of Preferences grant very limited preferential access to developing country exports, and even this can be withdrawn at short notice if the developing country actually succeeds in increasing its exports substantially

status[72]. The transition from central planning is no longer the defining feature or descriptive of the Central Asian countries' economic systems, but "transition" status allows the countries to be treated as non-market economies in anti-dumping determinations. In sum, developing country status may be difficult to negotiate and is scarcely worth the effort, while transition status may be difficult to shed but in view of the salience of anti-dumping measures as protective instruments it is definitely worth the effort.

KAZAKHASTAN

Before the republic of Kazakhstan state acquired state sovereignty, it had no experience in conducting foreign trade and hence lacked the conceptions institutions and personal need to perform this task. Instead the entire foreign economic activities of the enterprises of Kazakhstan, including foreign trade was handled by central all union institutions in Moscow. This did not mean that its foreign activity was marginal on the contrary, because the Kazakhstan was the part of the national economic complex of the USSR and because it was endowed with unique, rich mineral; resources it actively participated in the foreign trade of the former Soviet Union .Indeed the Kazakhstan occupied one of the leading places in terms of volume in number of goods – non ferrous material, rare and rare earth metals, Ferro alloys, chromites ore, and phosphorous. In the 1980s more than 180 enterprises were active in producing goods for export .Its array of export goods included about 200 items; the geographical destination for this goods included 80 countries around the world, with about 60% of the total volume of export going to countries in council in mutual economic assistance[73]

72 This may change since agreement was reached in 2002 as part of Russia's WTO accession negotiations that it be treated as a market economy. Transition status allows the importing country to disregard actual prices in the alleged dumping country when calculating dumping margins and instead to use constructed values, which are often biased in favour of the import-competing industry's claims.

73 N.Sh. Dulatov , *Vneshneekonomicheskie sviaz kazakhastana s zarubezhnymi stranami* (Alma-ata 1982*), pp 2-17 , 54*

Taking into account the starting point, one can conclude in relatively short period of time, Kazakhstan has been remarkably successful in its effort to gain access to world market. The foreign trade turn over has comprised a significant portion of the total volume of GDP rising from 55% to 75%[74]

FOREIGN TRADE STRUCTURE

In recent years, Kazakhstan has become more integrated into the world economy. Foreign investment has increased, especially in the oil and natural gas sectors. In 1994 Uzbekistan and Kazakhstan established a free-trade zone between the two countries, and Kyrgyzstan soon joined the agreement. In the same year, Kazakhstan signed a partnership accord that established economic contacts with the European Union (EU). In 1996, seeking closer economic integration with Belarus, Kyrgyzstan and Russia, the country approved an agreement on a common market and customs union. Kazakhstan has benefited from a surge in oil prices as well as higher oil and metals export volumes in 2000, with exports at their highest level since 1993. According to official figures, total exports on a customs basis reached US$ 9.1bn (49.9% of GDP) in 2000, up by 63.4% year on year. Recorded imports on a customs basis, which understate the true cost of imports, rose 10 to US$ 5.1bn (27.6% of GDP), a 37% year on year increase. Although customs figures imply a trade surplus of US$ 4.1bn (22.3% of GDP) in 2000, the actual trade surplus when measured on a balance of payments basis is likely to be closer to US$2bn-2.5bn (10.9-13.7% of GDP) [75]. Oil and gas condensate accounted for 52% of export earnings on a customs basis in the first eleven months of 2000, compared with 41% in the same period of 1999, which translates into a year on year increase of 120%. Ferrous metal exports were worth US$1,080m, up by 38% year on year and equal to 13% of total exports in the first half of 2000. The revenue from Grain export increased by 125% of US$ 462m, to about 6% of total

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74 Boris Rumer and Stanislav Zahukov ed, *Central Asia Challenges of Independence* (New Delhi, Aakar Books, 2003)

75 Sources: Gateway to Kazakhstan, "foreign trade", (wwww.kazakhstan-gateway.kz/index.php)

exports. This increase was attributable to a good 1999 harvest and a slight increase in grain prices.

Table 17: Foreign Trade, 2000 (US$ m unless otherwise indicated)

Exports fob	9,140
Imports cif	- 5,052
Trade balance	4,087
% of GDP	15.7
Main exports (% of total)	
Fuel & oil products	52.8
Ferrous metals	12.9
Copper	8.1
Chemicals	4.2
Grain	5.5
Main imports (% of total)	
Machinery	18.8
Fuel & oil products	11.3
Electrical equipment	8.8
Vehicles	8.7
Ferrous metals products	6.4

Sources: TACIS, Kazakstan Economic Trends.

The direction of trade is now thoroughly oriented towards Western markets and Caribbean markets. In the first half of 2000 Kazakhstan sold US$1,064 m in exports, 24.4% of total exports on a customs basis, to Bermuda and the British Virgin Islands, 327.2% more than in the year- earlier period. In the first half of 1999 these two Caribbean markets bought just 12.2% of all Kazakh exports on a customs basis. Almost all exports to Bermuda and the British Virgin Islands are of crude oil, so that, in the first half of 2000, 51.4% of all Kazakh fuel exports (oil, gas condensate, refined products and gas) exports went to the Caribbean compared with 35.3% a year earlier. The second largest export market is Russia, which took US$891.1m in exports on a customs basis in the first half of 2000, 21.1% of the total and a 114.9% increase year on year. Kazakhstan's two other main export markets are Italy and China. Italy bought US$330.9m in exports, all of which was oil sent to Italian oil terminals, in the first half of 2000, 7.9% of total exports on a customs basis. Exports to Italy rose by 94.8% year on year. China took US$319.3m in Kazakh exports in the first half of 2000, 7.8% of the total and a 25 year- on- year increases.

Table 18: Main Sources of Imports 2000 (% of total)

Imports(a) from:	
Former Soviet Union	54.6
Russia	8.8
Other	48.7
Germany	5.9
US	6.6
UK	4.3
Italy	3.1

(a) Recorded imports only.
Source: TACIS, Kazakhstan Economic Trends.

Kazakhstan's current account has swung from an unsustainable deficit to a surplus in just two years, thanks to the 1999 devaluation-which curbed import costs-and a recovery in oil prices accompanied by higher export volumes of the commodity. The devaluation of the Russian rouble in August 1998 pushed the current-account deficit to 10.6% of GDP in the fourth quarter of 1998 alone. The bulk of the current-account deficit in 1998 was made up of the deficit on visible trade. The devaluation caused a 13.8% fall in imports of goods and services costs in 1999 when compared with 1998. In 2000, however, exports of goods and services climbed by 55.3%, thanks mostly to higher oil prices and export volumes, causing a 5.9% of GDP current account surplus, the first since independence in 1991.

Table 19: Current Account, 2000 (US$ m unless otherwise indicated)

Exports fob	9,615.4
Imports fob	-6,849.8
Trade balance	2,765.6
Services credit	1,135.4
Services debits	-1,854.5
Services balance	-719.1
Net income balance	-1,178.8
Net interest balance	-1,052.6
Other income balance	-126.2
Current transfers	206.7
Current-account balance	1,074.4
% of GDP	5.9

Sources: IMF, International Financial Statistics

FOREIGN TRADE REGIME

Kazakhstan has now become a relatively open economy and has submitted an application to access the WTO in January 1996, with observer status at present. The government considers the accession to the WTO as a priority for external economic policy and is in the process of carefully examining and revising its trade policies. In order to become a member of the WTO, Kazakhstan needs to remove barriers to trade, establish competitive markets for both domestic and international goods, and discuss bilateral trade agreements with other WTO members. Kazakhstan started liberalizing its foreign trade in the mid-1990s. Market reforms undertaken during 1994-1997 enabled the government to continue major but gradual reforms in the foreign trade sector. In 2001, the shares of exports and imports in GDP were about 49 and 37 % in current prices, respectively, both significantly higher than in 1996. The average weighted tariffs were lowered to slightly less than 9 percent and the numbers of tariffs in excess of 20 percent were cut by more than half. The applied average weighted import tariff decreased to 9.8

percent in 2000[76]. Trade liberalization in Kazakhstan coincided with a deep economic decline, and the majority of the public believes that trade liberalization was one of the major causes of the decline. The financial crisis of August 1998 resulted in an introduction of provisional tariff and non-tariff regulations with the aim of protecting the domestic market from dumping and quantitative imports, which greatly damaged local producers. So, import substitution policy became the most dominant strategy of policy makers after shock on domestic producers in 1998. One of the basic policy instruments which were proposed under this program was the wide implementation of safeguard, anti-dumping and countervailing tariffs on imported goods, agricultural and non-agricultural. Simultaneously Kazakhstan continued work on accession to the WTO by active and full-scale bilateral and multilateral negotiations. Four rounds of bilateral negotiations have been conducted, both being aimed at discussing the initial proposals made by Kazakhstan and connected with the availability of market access for goods and services. The central point of a country's liberalization commitments in the WTO are tariff bindings, which are commitments by a member not to raise its tariffs beyond "bound" level without consulting and/or compensating its trading partners. At the fourth meeting of the Working party (2002) Kazakhstan presented its offers on market access for: (I) Agricultural Products and (II) Non-agricultural Goods. More than 80 % of the tariff nomenclature for agricultural products and more than 70 % of the tariff nomenclature for industrial products were revised and significantly reduced. The number of tariff peaks has been considerably decreased. The implementation period for all tariff positions has been also reduced. Two possible shocks due to trade policy changes are described: the first is import substitution policy and increasing tariff rates, the second is accession to the WTO and trade liberalization.

[76] Saule Kazybayeva (Consultant) and Aysen Tanyeri-Abur (FAO) Trade Policy Adjustments in Kazakhstan:A General Equilibrium Analysis Contributed paper presented at the International Conference Agricultural policy reform and the WTO: where are we heading? Capri (Italy), June 23-26, 2003

The most significant outcome of access to the WTO for Kazakhstan is a reduction in government revenue. The relative importance of this result seems to be strengthened in the case of economic crisis, or fall of world prices of important export commodities (oil, metals, and wheat). Another reason is that the government intends to reduce the value-added tax in 2003 in order to reduce the tax burden on consumers. Scarcity of budget resources can negatively influences low-income households, which highly depend on government transfers. There is a difficulty to reduce current expenditures of the government of which about 50% are civil wages (they are already very low). From the revenue side an increase of the corporate tax can be considered as a possible way to compensate government losses without significant distortions in market prices. The increase of corporate tax was examined in a counterfactual scenario to find the appropriate level at which impact on economic activity of sectors is minimal .The focal point was to reach the benchmark value of state revenue. The simulations result in a 15 % increase of initial level corporate tax that can be optimal in terms of trade liberalization and access to the at the macro level, GDP decreases, as expected, under a regime of the import substitution policy and the imposition of higher import tax. Unemployment increases and household income is reduced. On the other hand, adjustment through the reduction of tariffs to a lower rate under trade liberalization leads to an increased; GDP reduced unemployment and improved households' welfare, also as expected .These favorable results, however, are counterbalanced by the loss in government revenue. It suggests the need to implement a higher tax on corporate income if the government revenue is to be protected as the country's trade regime is being liberalized .Another finding is that the overall impacts of trade liberalization through the tariff reduction in the model is relatively small for Kazakhstan. The first reason is that Kazakhstan has already experienced significant liberalization of foreign trade (including agricultural sector) and the applied tariff is considerably lower than in most of developing countries. The free trade agreement between members of the CU is also an important part of the trade liberalization in Kazakhstan. The other reason is that the collected customs duties are less than they should be because of exemptions existing for some big importing companies, shuttle imports and low quality of tax administration Results of the study on impacts of liberalization in each sector on economic activity and household's welfare indicate that trade policy adjustments to each sector influence economic activity not only in that sectors but also in the other sectors, including non-tradable activities. Trade liberalization in agriculture results in the most significant impact on GDP. Liberalization of trade policies in the food industry affect domestic prices less, due to the lower share of this sector in foreign trade and the small share in intermediate consumption. Total output in the food industry sector Nevertheless, the overall effect in the economy is more favorable when all market shares liberalized. On the other hand, imposition of tariffs in the food industry leads to decreasing income, and also food consumption of households. This results in a considerable negative outcome for the low-income categories of households. Turning to the household welfare it was found that the trade adjustments in the industry have more important influence on the household income. Households suffer relatively higher income losses in the case of industry protection compared to protection in other sectors and gain more in the case of liberalization of the industry. These results from CGE analysis lead to conclude that the import [77]substitution policy adversely affects the economic growth and penalizes households, while the trade liberalization is more preferable for economic activity and increases over all welfare. This conclusion has relevance for Kazakhstan in view of the growing protectionist pressure in the last years and the wide discussions on the accession to the WTO.

Factors Attributing Kazakhstan To Market Economy

Several factors attribute to recognition of Kazakhstan as a market economy:

[77] Trade Policy Adjustments in Kazakhstan:A General Equilibrium Analysis Saule Kazybayeva (Consultant) and Aysen Tanyeri-Abur (FAO) International Conference Agricultural policy reform and the WTO: where are we heading? Capri (Italy), June 23-26, 2003

(i) The extent to which Kazakhstan's currency is convertible into the currency of Other countries;

(ii) The extent to which wage rates in Kazakhstan are determined by free bargaining between labor and management;

(iii) The extent to which joint ventures or other investments by non-Kazakh firms are permitted in Kazakhstan;

(iv) The extent of government ownership or control of the means of production;

(v) The extent of government control over the allocation of resources and over the price and output decisions of enterprises;

(vi) Other factors as appropriate.

Each of the six factors is framed in terms of "the extent" to which the transition has been made, "suggesting that complete *laissez faire* or a perfectly competitive market economy is not the applicable standard." Kazakhstan has received repeated commendation by numerous international organizations and observers for the progress it has made since the break-up of the Soviet Union in implementing the legal framework and institutions of an economy based on market principles. Kazakhstan's Currency, the *Tenge*, is Convertible into the Currency of Foreign Countries. Kazakhstan's currency, the *tenge*, is freely convertible. As a member country of the International Monetary Fund ("IMF"), Kazakhstan has acceded to the requirements of Article VIII of the IMF Articles of Agreement regarding current-account convertibility, making its exchange system free of all restrictions on payments and transfers for current international transactions[78]. The Department itself, in its Kazakhstan Year 2000 Investment Climate Statement, described the legal framework in Kazakhstan as providing for currency convertibility[79]Foreign investors in Kazakhstan are allowed to open and maintain accounts in foreign currency, pay debts in foreign currency, and freely

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78 IMF, *Republic of Kazakhstan—Staff Report for the 2000 Article IV Consultation*, SM/00/257, November 17, 2000 (hereinafter "IMF Staff Report")

79 Kazakhstan: Year 2000 Investment Climate Statement, BISNIS, U.S. Dept. of Commerce, 13 September 2000 (hereinafter "DOC Investment Statement").

convert and repatriate profits earned in Kazakhstan. Residents of Kazakhstan may also apply for a license to move capital outside the country in foreign currency. Within Kazakhstan, there are no restrictions on foreign currency exchanges through banks and other organizations. Kazakhstan's currency has also remained relatively stable, even as the rest of its neighbors were suffering the effects of regional financial crises. The *tenge* was allowed to float and underwent devaluation in April 1999 in reaction to the Russian and Asian financial crises. That move was lauded by international financial organizations and the *tenge* quickly stabilized thereafter[80]. Kazakhstan's inflation rate is better than many more-industrialized countries at an average of 6.7% for 1998 and 1999 (by comparison, Russia's rate for the same period was 63.9% and the Czech Republic's was7.6%)[81]. Low inflation is attributable to Kazakhstan's stable currency and tight fiscal policy[82].The IMF classifies Kazakhstan's exchange arrangement as "independently floating," meaning that the exchange rate is market-determined with minimal intervention aimed only at moderating the rate of change and preventing undue fluctuations rather than establishing a set exchange rate level. The exchange rate for the *tenge* depends entirely on supply and demand on the foreign exchange market, and the National Bank of Kazakhstan ("NBK") will not substantially intervene in setting the exchange rate[83]. The exchange rate is determined on the basis of inter bank foreign exchange auctions now held daily. The currency market consists of over-the counter inter bank exchanges at freely negotiated rates, as well as the Kazakhstan Stock Exchange (KASE) which conducts trading[84] Kazakhstan's gold and currency reserves are no longer used to

80 Freedom House, *Nations in Transit 2000: Kazakhstan*, avail. at http://www.freedomhouse.org (herein after "Freedom House Report"), "Introduction."

81 ibid

82 Economist Intelligence Unit (EIU) Country Report: Kazakhstan, April 10, 2001, "Overview."

83 OECD GLOBAL FORUM ON INTERNATIONAL INVESTMENT New Horizons and Policy Challenges for Foreign Direct Investment in the 21st Century *26-27 November 2001, Mexico City, Mexico*FOREIGN DIRECT INVESTMENT IN KAZAKHSTAN1 available at www.oecd.org

84 ibid.

control exchange rate levels. Kazakhstan is likely to meet all of the fiscal targets set with the IMF thanks to its tight fiscal stance, high oil revenue, and rapid economic growth. Kazakhstan has paid off all of its outstanding IMF debt and has not needed to draw on the extended fund facility negotiated in December 1999[85].

Kazakhstan Welcomes Foreign Investment

Joint ventures and other foreign investments into Kazakhstan are not just permitted but actively encouraged. Among all the countries of Eastern Europe and the former Soviet Union, Kazakhstan is one of the most open toward foreign investment. Foreign direct investment (FDI) in Kazakhstan averaged $966 million, or $63 per capita, in 1998 and 1999[86]. In 1999, Kazakhstan ranked third among former socialist-bloc countries in terms of total volume of foreign investment at $1.5 billion, behind only Poland and Hungary. In 2000 FDI rose to 2.7 billion USD, in 2001 the Government forecasts further increase to 3.5 billion USD.

All sectors of the economy are open to foreign investment[87] and foreign investors are allowed to participate in privatization[88]. Foreign investors are involved in the energy sector, the steel industry, extraction industries, and many other sectors. Laws on foreign investment, the Agency of the Republic of Kazakhstan for Investment (ARKI), and the Foreign Investors' Council all encourage and support foreign investors. The Law "On Foreign Investment" (27 December 1994) protects foreign investors from nationalization/expropriation, changes in legislation, and illegal action by state agencies or officials and guarantees the unrestricted use of income and currency convertibility for dividends and other uses[89].17 In addition, the Law "On the State Support of Direct

85 EIU Country Report, "Foreign trade and payments."

86 ibid

87 OECD GLOBAL FORUM ON INTERNATIONAL INVESTMENT New Horizons and Policy Challenges for Foreign Direct Investment in the 21st Century *26-27 November 2001, Mexico City, Mexico* FOREIGN DIRECT INVESTMENT IN KAZAKHSTAN1 available at www.oecd.org

88 ibid

89 IBRD Memo at 69-70.

Investment" grants state assets and concessions, income, land and property tax holidays for five years with additional periods at reduced rates, plus duty and VAT exemption for imported machinery and inputs for varying periods. Furthermore, foreign investors may own and lease land according to the Law "On Land" (24 January2001)[90].

Other Factors Also Indicate Kazakhstan's Progress In Market-Based Reform

One should consider Kazakhstan's openness to foreign trade and integration into the global trading system, its considerable progress towards accession to the WTO, its emergence on global capital markets along with the United States' considerable investment in its economy, its comprehensive tax system based on international models, and its enactment of national competition laws and improving judicial system as compelling further evidence of Kazakhstan's status as a market economy country.

Kazakhstan has demonstrated its openness to foreign trade through its substantial integration into the international trading system. From 1994 to 2000, the value of its exports rose from US$3.23 billion to US$9.14 billion. In that same period, the value of its imports grew from US$3.56 billion to US$5.05 billion.[91] Moreover, during that period, the geographical distribution of Kazakhstan's exports and imports moved decidedly away from the original emphasis on trade with countries of the Baltic's, Russia, and the Other States of the former Soviet Union ("BRO"). In 1995, trade with non- BRO countries constituted only 41.89% of Kazakhstan's exports and 29.36% of its imports. By 1999, Kazakhstan's trade with non-BRO countries had risen to 69.90% of its exports and 56.31% of its imports. These percentages include 22.9% of exports to, and 25.3% of imports from, the EU.[92] This trend demonstrates that Kazakhstan has moved away from a

[90] World Bank, "Kazakhstan: Joint Private Sector Assessment," available at http://www.worldbank.kz/content/esw7_eng.html.

[91] International Monetary Fund, *International Financial Statistics*, May 2001 at 17.

[92] EIU Country Report, "Economic Structure."

lingering reliance on trade with countries of the former Soviet Union and toward trade with many of the other market economies in the multilateral trading system that Kazakhstan has entered. Kazakhstan has conformed its trade regime to WTO standards, completed the first round of WTO accession negotiations in 1997, and second round – in 2001 and expects to be admitted to the WTO in the very near future. Kazakhstan has liberalized its trade policies and belongs to several international trade organizations. Kazakhstan has no export tariffs. In 1998, Kazakhstan issued a resolution that decreased its average import tariff rate to 9%. Although some temporary trade barriers were erected in 1998 against imports from neighboring countries in response to the collapse of the currencies in those countries, most of these were removed in June 1999. Furthermore, Kazakhstan has adopted the international tariff nomenclature as the basis of its tariff schedule, and its customs valuation rules conform to the WTO Valuation Agreement.[93] These measures demonstrate the depth to which Kazakhstan has embraced the market-based international trading system. Through its openness and growing international trade, Kazakhstan industries are now competing in the global market economy. Kazakhstan has established the framework and infrastructure for functioning capital markets, founding the National Securities Commission in 1995 and passing its Securities Law in 1997.[94] Kazakhstan has issued Eurobonds on the international market. It has promoted foreign investment into its new market economy and the United States has signaled its response to the market opportunities in Kazakhstan. The United States accounted for 50.17% of the foreign direct investment in Kazakhstan in 1999[95] and 36% in 2000. Kazakhstan's presence within the global financial system provides further evidence of the liberalization and stability of its new market economy. Moody's has assigned

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93 *See* U.S. Department of State FY 2000 Country Commercial Guide: Kazakhstan at Ch. VI.

94 OECD GLOBAL FORUM ON INTERNATIONAL INVESTMENT New Horizons and Policy Challenges for Foreign Direct Investment in the 21st Century *26-27 November 2001, Mexico City, Mexico* FOREIGN DIRECT INVESTMENT IN KAZAKHSTAN1 available at www.oecd.org

95 *See* January 2001 IMF Country Report No. 01/20

Kazakhstan a B1 rating, equivalent to that of Argentina, and better than the ratings assigned to Bulgaria, Romania, Russia, and the rest of the countries in the CIS.[96]Kazakhstan's new Tax Code is considered by tax experts to be among the most comprehensive in the region, applying an international model based on principles of equity, economic neutrality, and simplicity.[97] Although challenges remain to the effective administration of its tax system, Kazakhstan has implemented a tax system appropriate for a market economy. In addition, the Government is in the process of revising the tax code so that it will contain detailed instructions on procedures, with the goal of improving implementation.[98]

Kazakhstan's achievements during its 10 years of independence demonstrate to international investment community its ability to be a reliable partner bearing great economic potential. Based on the factors mentioned above it should be recognized that during these years the country has managed to build a solid foundation for open market economy. As Kazakhstan starts looking into the next decade of its sovereign development, country's vulnerability to external shocks, similar to the one in 1998-99, will be diminished significantly due to a stronger and more resilient balance of payments position, improved fiscal flexibility, excellent prospects for oil export growth, resulting rapid decline in the country's debt levels and a medium-term political stability and reform continuity. At the same time, in the longer term in the next decade the potential for rapid development remains good. Although some weaknesses will remain in short to medium term given that economy is largely dependable on revenues from oil and minerals exports, which makes it vulnerable to external price shocks, Government remains committed to further reforms aimed at promoting economic prosperity and wealth through the development of modern and diversified economy.

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96 IMF Staff Report, Statistical Appendix at 20.

97 DOC Investment Statement ¶ 8.

98 IMF Staff Report at 16

KAZAKHSTAN AND THE WTO

The accession process

At present, the Republic of Kazakhstan negotiates its accession with the WTO members. The Kazakhstan's WTO Accession Working Party was established on 6 February 1996. Bilateral market access negotiations in goods and services commenced in October 1997, and are continuing based on a revised goods offer and the existing services offer. Topics under discussion in the Working Party include: agriculture, the customs system (and customs union arrangements), price controls, import licensing, industrial subsidies, SPS and TBT, transparency of the legal system and legislative reform, services and TRIPS. In order to join the WTO, Kazakhstan is required to complete three "phases" of accession:

1- Completion of a Memorandum on Foreign Trade Regime which describes trade policies and institutions,
2- Once the Working Party has made sufficient progress on principles an trade regimes[99] ,
3- Bilateral negotiations with interested WTO members begin: each WTO member is entitled to undertake bilateral negotiations for increased market access and reductions in trade restrictions with the applicant. In this sense, the negotiations are unidirectional, because only the members make demands during the negotiations. Once the negotiation is concluded, the country is invited to join the WTO[100] Since Kazakhstan introduces its application for accession to the WTO, it has accomplished a great work in bringing its foreign trade legislation into conformity with the WTO rules and principles. On market access negotiations, its tariffs binding has been revised and reduced based on

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[99] The Working Party goes into the substantive part of the multilateral negotiations involved in accessions. This phase determines the terms and conditions of entry for the applicant government. Terms and conditions include commitments to observe WTO rules and disciplines upon accession and transitional periods required making any legislative or structural changes where necessary to implement these commitments.

[100] Refer to the WTO web site under the rubric "Accession" (www.wto.org)

the suggestions formulated by the WTO members. The implementation period for all tariff position has also been reduced. At the Fourth Ministerial Conference in Doha, the Minister of Economy and Trade of Kazakhstan stated that "The prospects for development of the Kazakhstan economy in many respects depend on overcoming crisis situations in certain industries, structural reorganization and completion of reforms. Therefore for Kazakhstan it is extremely important that WTO Members refrain from requesting from Kazakhstan overly rigid and excessive commitments, as compared to the obligations of existing WTO Members, so that Kazakhstan can provide necessary levels of tariff protection for sensitive sectors and develop the infant-industry sectors of its economy"

Concerns of the Business Community[101]

At present, the business community needs more information about all aspects of the WTO accession process, especially about the new business opportunities and challenges which may result from the country's WTO membership. Most of business people are interested in the WTO accession process of Russia and other CIS countries. The business community is of the view that WTO accession of neighboring countries will have a positive impact on conducting business in the region. Producers stress that production in the light industry, but especially in the textile and clothing sector has dropped sharply in the last several years. Business people also face imports of low-priced and bad quality products causing substantial damage to the domestic industry. Finally, conditions of transit through other CIS countries are unpredictable which a serious burden on exports and imports is. The business community needs a more active dialogue with the government in matters, which are related to the WTO accession of the country.

[101] Section based on the Action Plan of ITC's World Tr@de Net Programme (www.intracen.org)

Priorities in export policy[102]

Kazakhstan's current export profile requires a trade policy, which simultaneously seeks to improve the competitiveness of its basic export goods and to develop non-conventional new goods for export requiring a high level of processing. The basic priorities of Kazakhstan's export policy are:

Contributing to steady growth of export by:

- Extension of commodity markets
- Concluding bilateral and multilateral agreements on trade
- Removal of present discriminatory barriers against Kazakhstan goods by negotiations
- Increases in delivery of traditional Kazakhstan export goods
- Development of external market for new non-traditional goods.

Maintaining maximum returns from exports to be used for export policy by:

- Treaties against double taxation
- Ending the system of controlling foreign trade contracts aimed at reducing the taxable basis
- Sanctions against exporters who abuse international practice and local laws.
- Banning ungrounded limits on the export for Kazakhstan goods
- Ensuring that reforms of the economy are strictly implemented. These priorities will be realized through:

a) The expansion of credit and export insurance, information and reviews of new markets, and strengthening of the statutory base for meeting the conditions of world trade
b) Export policy measures to reduce the risks from commodity market volatility
c) Creation of an export development programme

[102] Country Paper on " Problems and prospects of export development for the Republic of Kazakhstan, web site of the International Trade Centre under executive forum 2001.

d) Establishing the legal basis for the development of electronic commerce Use of tools such as credits and incentives to persuade domestic exporters of raw materials to switch to goods with high added value
f) Defining the terms for an organization devoted to trade development (OCDT). One of its main activities will be the organization of a system of credits and export guarantees.

Benefits of acceding to the WTO

Generally speaking, the Republic of Kazakhstan will benefit from its accession to the WTO system. Firstly, WTO membership requires that domestic policies be consistent with international practice through the development of internal institutions and a reduction of the role of government in the economy. Therefore, the participation in the multilateral trading system could provide better legal standards and a push toward the development of a market based economy. More specifically, the membership of the WTO would give the country the following advantages:

- access to new markets for exporting goods and services;
- introduction of non-discriminatory trade regime for goods in the markets of importer countries;
- more attractive, stable and predictable conditions for investments;
- broader assortment of better quality of goods and services at lower prices for consumers;
- access to an efficient dispute settlement mechanism;
- bringing trade, investment and customs regulations into accord with international standards;
- freedom of transit through territories of WTO member countries;
- better access to world market information.

Since its independence from the former Soviet Union in 1991, the Republic of Kazakhstan has made remarkable progress in achieving market-oriented economic reforms and macroeconomic stabilization. Today, measured by any of a variety of yardsticks, Kazakhstan should be rewarded for its progress during ten years of independence and recognized by the world community as a market economy. Market-oriented reforms achieved by Kazakhstan include: a freely convertible, and now[103] more stable, currency, the *tenge*; legal guarantees to workers of the rights to organize in trade unions and collectively bargain as well as the reality of rising real wage rates (and declining unemployment); price and interest rate liberalization; substantial privatization of small- and medium-scale enterprises and of many of the largest enterprises; the elimination of trade distortions such as quantitative restrictions and pronounced integration into the international trading and investment systems; the introduction of new laws, including a tax code based on international standards, an effective bankruptcy law, laws on competition and the securities market, and other components of the essential legal framework for a market economy. Kazakhstan's progress in creating a young and growing market economy, although substantial, is ongoing and has not been achieved without a share of difficulties. Kazakhstan's new market economy faces some continuing transition challenges which remain to be met before it can fully realize the economic fruits of its market-based liberalization process. The likelihood that Kazakhstan will continue along the path of transition is high. The stated long-term priorities of the Government of Kazakhstan are consistent with the role of government in an economy that is completing its transition to a market system. Among those stated priorities, spelled out in *Kazakhstan 2030—Prosperity, Security and Improvement of the Welfare of All Kazakhstani People*, is the following (one of seven "key goals"): "Economic growth based on an open-market

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[103] OECD GLOBAL FORUM ON INTERNATIONAL INVESTMENT New Horizons and Policy Challenges for Foreign Direct Investment in the 21st Century *26-27 November 2001, Mexico City, Mexico* FOREIGN DIRECT INVESTMENT IN KAZAKHSTAN1 available at www.oecd.org

economy with" Kazakhstan has been a leading reformer in Central Asia in the decade since its independence in 1991. In recent years, market-based government reforms have stabilized the macro economy, liberalized the financial sector, transformed the pension system, and restructured the public sector. In the aggregate, price liberalization has created a framework where economic agents now respond to market signals in Kazakhstan. Further, as a consequence of the substantial privatization process, the level of foreign direct investment in Kazakhstan is one of the highest among all of the former Soviet bloc countries. In year 2000 it reached 2.7 billion. While the pace of structural reform in some areas of the economy slowed during 1998 under the strains of declining oil prices, a drought-induced domestic grain shortfall, and the lingering effects of regional financial crises, "the process of market-oriented reform is now seen to be irreversible." The twin shocks of the Asian and Russian financial crises in 1998 interrupted the first modest economic growth that Kazakhstan had achieved since independence. Due primarily to the mass privatizations and other market-based reforms that had been completed by the mid-1990s, Kazakhstan's progress allowed it to realize positive GDP growth in 1996 and 1997. At the same time, unemployment had steadily fallen to less than seven percent and single-digit inflation was achieved by 1998. In spite of the economic progress made to that point, Kazakhstan's GDP growth declined in 1998 as a result of the regional financial crises. Notwithstanding the tremors from these economic shocks, which temporarily diverted the government's attention from its ongoing market reform and privatization goals, the government followed through with its decision to allow the *tenge* to freely float (which completed the *tenge's* procession to full convertibility). As a testament to the market-based reforms Kazakhstan had already accomplished by 1998, it recovered from the 1998 crisis quickly and achieved positive GDP growth again in 1999, which increased dramatically in 2000by 9.6%. After a decline in 1998, the level of foreign direct investment has also been reinvigorated; inflation, unemployment and the exchange rate have all been stabilized at sustainable levels; and the government has renewed the final stages of market reforms including the final stages of privatization focused on large-scale enterprises. Kazakhstan's recovery from the 1998 shocks and its decision to embrace the remaining elements of market reform show that its fledgling market economy exists within a structural framework evidencing the political will to further develop and grow within a market-based economic system.

UZBEKISTAN

Integration of Uzbekistan into the world economy is one of the main directions of reforms implemented in the country. Therefore, introduction of common standards set forth by WTO into the country foreign trade practice is one of the important aspects for attaining planned targets.

The Republic of Uzbekistan has achieved tangible success in this process. During the independence period the strong legal base has been formed to support economic reforms including those that anticipate far going liberalization of foreign trade regulation, creation of favorable conditions for foreign trade activity.

Yet, to assess more precisely country's potential capacity for accession to WTO one should determine the adequacy of the foreign trade regime to WTO agreements through analysis of legislation on foreign trade regulation and relevant economy sectors. World Trade Organization represents the global legal and institutional mechanisms established[104] for liberalization and unification of trade regimes in sovereign states based on multilateral agreements.

Agreement on WTO establishment includes 29 juridical documents that cover practically all spheres-from agriculture to textile and clothes as well as norms regulating commodity origin and intellectual property. Besides, there exist more than 25 declarations, decisions and agreements at the level of ministries that formulate additional obligations and rules that all WTO members are to assume.

[104] Muradova Kh.,Khusnia@cer.uzAbdurazakov A .Uzbekistan, Center for Economic Research, Ref.#1188, N72 -Selected Papers "Foreign Trade Regime of Uzbekistan and Its Compliance to Norms of Agreements of WTO" Available at www.gtap.agecon.purdue.edu/resources/download/1834pdf

WTO declares that provisions of international agreements dominate over national legislation. WTO rules, contained in international agreements, considerably restrict opportunity for direct government intervention in the national economy, including implementation of traditional industrial policy, and make government highly responsible for violations of these rules.

WTO rules demand that country should allow considerable and irreversible trade regime liberalization, ban subsidies and price restriction (fixation) prohibited by WTO rules, protect intellectual property rights, follow requirements on trade regime transparency and accountability for WTO Extent of economy adaptation (openness), trade regime in particular, to WTO rules and norms is determined by the broad terms of economic legal base and existence of relevant mechanisms ensuring full-range functioning of principles and agreements within WTO framework[105].

FOREIGN TRADE STRUCTURE

Exports

Uzbekistan still remains exporter of primary goods and raw materials. Main item of exports are cotton 41.5%, gold 9.6%, energy products 9.6%, mineral fertilizers, ferrous metals, textiles, food products, automobiles[106] . Economy of Uzbekistan is gradually undergoing a slow change[107].While retaining its traditional position in the world market for raw stuff, domestic manufacturers are doing their best to intensify exports of products with a higher level of processing as a result the share of raw material in composition of Uzbek export tend to shrink, with the share of the manufacture, goods, completing parts, mechanisms, machinery and equipment are rising steadily. The export of the chemical products, machinery and equipment has increased twice as much. The physical volume of exported cotton

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105 ibid

106 http://www.cia.gov/cia/publications/factbook/geos/uz.html

107 SWB/SU/1465 G/3 12 JANUARY 2001

remains unchanged its proportion has fallen to 18.1% , (to compare , the year 2003 saw a19.1% fall) simultaneously the export volume of textile produced including yarn , cotton , fabrics , knitted wears and garments have increased by 25%. Main export partner of Uzbekistan are Russia 21.2%, China 14%, Ukraine 7%, Turkey 6.3%, Tajikistan 5.8%, Bangladesh 4.2% (2004)[108] .Uzbek government is trying to encourage the export of manufactured goods which can generate more revenue and boost economy. Uzbekistan is trying to access new market and with this intention it is trying to establish economic links with other countries.

Imports

Uzbekistan after independence has not been self sufficient in production of various commodities of daily needs. Thus it imports commodity of daily needs. It also imports machinery and equipment 49.8%, foodstuffs 16.4%, chemicals, metals[109]. Main Imports partners of Uzbekistan are Russia 26.4%, South Korea 10.8%, Germany 9.4%, China 8.3%, Kazakhstan 6%, and Turkey 6% (2004).

Despite a certain rise in both in physical and cost volume in goods imported on to the republics territory no significant change in the composition has occurred. Machinery and equipment represent a lion's share of Uzbeks share import: 44% with chemical produce and plastic accounting for: 13% services: 12.1% ferrous and non ferrous metals and produce made their off: 10.9% food stuff 6.8% fuel 2.2% and other commodity groups 11.3%: such a stable import composition that remains practically unchanged in the course of several years clearly demonstrates the home market the permanent demand for these product categories imported to Uzbekistan.

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108 http://www.cia.gov/cia/publications/factbook/geos/uz.html

109 ibid

FOREIGN TRADE REGIME

Foreign trade policy of each state is guide first and foremost by the aim of integrating into the system of international economic relation. It is designed to ensure the realization of following task.

- to stimulate the inflow of foreign investment
- ensure the maximum utilization of local raw materials
- to facilitate the creation of additional job while protecting the existing ones
- to create competitive environment in the home market place the foreign trade regime
- to address a number of fiscal tasks associated with the 'replenishment of the state's budget revenues[110].

The effective application of internationally recognized trade policy instruments should foster the Republic's economic growth as a whole, and thereby deliver tangible improvements in the living standards of its population. The foreign trade regime established in the Rppnhlie-ef Uzbekistan is -characterized by a sufficient level of openness, as well as by the absence of such Clements as quantitative restrictions, quotation and licensing the export of goods (works or services) is fully exempt from customs payments. Moreover, domestic exporters are granted a number of privileges, including:

- exports customs duties on all sorts of goods (works or services) are abolished;
- goods (works or services) exported for freely convertible currency, including deliveries to the CIS member states, are subject to the imposition of value-added tax at the zero rate;
- exports of goods for freely convertible currency are exempt from excise tax;

[110] The material has been provided by the Agency for Foreign Economic Relations of the Republic of Uzbekistan.

- manufacturing enterprises have the right to export their produce without effecting prepayment and opening a letter of credit, provided that there are appropriate guarantees from authorized banks servicing the buyers;
- for domestic enterprises exporting their produce, the following procedure for paying income (profit) tax and property tax is established: in cases where the share of goods (works or services) exported for freely convertible currency varies from 15 per cent to 30 per cent of the enterprise's total sales volume, the fixed rates of income (profit) tax and property tax are reduced by 30 per cent; in cases where the share of exported goods (works or services) exceeds 30 per cent, the established rates for income (profit) tax and property tax are halved.

A new customs tariff is effective in Uzbekistan starting January 1, 2004. The calculation of rates for customs duties imposed on various commodity groups and sub-groups is based on the escalation principle, i.e. the higher the added value of imports, the higher the customs duty rate. The categories of goods previously taxed at the zero rate as well as those taxed at the maximum, 30 per cent rate, have been changed most of all. The point is, a considerable portion of these categories is now subject to taxation at a new 5-per cent rate. The arithmetic-mean rate of the new tariff is decreased to 14.6 per cent against the 15.4 per cent that was in effect earlier. In accordance with the customs regime classification depending on the level of average tariff rates used by the International Monetary Fund to assess the extent to which trade regimes in different countries are opened, the Republic of Uzbekistan's trade regime may be classified as "relatively opened" (the arithmetic-mean rate should be in the range of 10-15 per cent)[111].

To compare, the arithmetic-mean rate of customs tariff used in India reaches 32 per cent, in Pakistan — 20.4 per cent, in Mexico — 16.5 per cent, in the Russian Federation — 14 per cent, in Korea — 13.8 per cent, in Bulgaria —

[111] ibid

12.4 per cent, in Ukraine — 10.54 per cent and in China -1-0.4 per cent. At the same time, the majority of these countries are WTO members[112].

The average-weighted tariff calculated in conformity with a method specified by the World Trade Organization, amounted to 2.03 per cent in 2003, which, according to WTO classification, characterizes the tariff regime of Uzbekistan as "opened" (the average-weighed tariff is below 10 per cent). Under this method, the amount of collected customs duties is divided by the total value of taxed imports (excluding the positions taxed at the zero rate), taking into consideration a package of systemic privileges established in Uzbek law for the payment of customs duties[113]. The opened character of customs tariff is explained by the availability of a whole series of lavish incentives and privileges associated with the payment of customs duties.

In particular, the following commodity groups are not subject to the imposition of import customs duties:-

- goods originating and imported from countries, with which the Republic of Uzbekistan maintains the free trade regime (in 2003, goods imported from those CIS member states that enjoy "the most favored nation" status, accounted for 38.3 per cent of the total volume of imports to the Republic);
- goods delivered under intergovernmental and credit agreements signed on behalf of the Government of the Republic of Uzbekistan or against its guarantees; - goods needed for the implementation of investment projects, which are financed out of foreign credits supported by the Uzbek Government's guarantees;
- property imported to the Republic of Uzbekistan by foreign investors to meet their own production needs;
- goods imported by foreign investors as their contribution to authorized capital of enterprises set up with a share of foreign investment;

112 ibid

113 ibid

- technological equipment imported onto the territory of the Republic of Uzbekistan;
- equipment imported to the Republic of Uzbekistan in order to create computer data transmission networks, as well as computers and completing parts thereto, and software;
- equipment imported by small businesses in order to outfit their production facilities;
- imported wood and timber;
- imported materials and components, which are not produced domestically and used in the technological processes to manufacture localized produce by enterprises that are involved in the realization of projects included into the Localization Program.

In addition, several categories of imports are exempt from value-added tax. These include, in particular:

- technological equipment imported to the Republic of Uzbekistan for the following purposes:
- to equip the priority installations included into the Investment Program;
- to realize the investment projects financed by foreign credits extended against the Uzbek Government's guarantees;
- to outfit the newly-built and reconstructed enterprises specializing in the production of consumer goods;
- to contribute to authorized capital of enterprises with foreign investment (imported by foreign investors);
- equipment, materials (works or services) imported by legal entities, including nonresidents of the Republic of Uzbekistan, at the expense of loans and grants given by international and overseas governmental, financial and economic organizations under agreements signed by the Republic of Uzbekistan;

- equipment imported to the Republic of Uzbekistan to create computer data transmission networks, computers and completing parts thereto, as well as software;
- imported medicines and articles used for medical purposes.

In order to protect the population's health and safety, certain goods imported onto the territory of the Republic of Uzbekistan are subject to mandatory certification to ensure their correspondence to internationally accepted standards. Such protective measures are in line with Article 2.2 of the WTO Agreement on Technical Barriers in Trade, which allows the introduction of appropriate technical regulations to protect health or safety of people, lives or health of animals or plants, or to preserve the environment[114].

Japan, for instance, applies far more rigid measures for these purposes. Pursuant to Articles 6272 of the country's Law, "On customs", any individual or legal entity wishing to import goods to Japan, is obliged to submit a declaration to the customs office's director-general and to obtain an appropriate imports permit following the careful examination of goods to be imported.

In China, to cite another example, all imported goods should undergo a mandatory examination procedure at the State Quarantine and Certification Bureau, for which purpose the importer is required to present a certificate of correspondence for all imports[115].

To ensure the creation of propitious conditions for the importation of such produce, the state authorities of the Republic of Uzbekistan recognize such documents as examination and pre-dispatch inspection acts issued by independent consulting companies, which are accredited with Uzstandart. At present, these include the following world renowned companies: SGS, ITS, OMIC, CONTROL, Union plus a number of domestic firms.

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[114] ibid

[115] ibid

With a view to optimizing the imports certification process, the Cabinet of Ministers of the Republic of Uzbekistan has passed the Resolution No 38 on July 6, 2004. According to a given document, a list of produce subject to the mandatory certification procedure is curtailed by one third, in comparison with the earlier effective one. Similarly, for the purpose of ensuring that imports meet the established safety requirements and the interests of Uzbek consumers are protected, certain categories of consumer goods imported to the Republic of Uzbekistan should be labeled with appropriate notices in the official language. The requirement to label imports in the official language has been introduced in accordance with the Law of the Republic of Uzbekistan, "On protection of consumer rights" (Article 6), which lays down, in particular, that the producer (executor or seller) is obliged to provide consumers with the required, authentic and accessible information on goods (works or services) offered for sale. For example, in France, the labeling of a certain group of goods in the official language is an obligatory requirement. Kazakhstan has banned the sale of a selection of goods, if their labels (tags, packaging or instructions) don't contain the following information in both the official and Russian languages: 1) the title of commodity and its country of origin; 2) its manufacturer, date of production and the sell-by-date; 3) terms of storage, ways of application and nutrition value.

Prospects for foreign trade development in the Republic of Uzbekistan

While remaining true to the fundamental principles that underlie the development of its foreign economic relations, Uzbekistan will be consistently pursuing the "open door" policy in the external trade domain. With its foundations being laid down at the initial stage of economic reform, the policy aims to ensure a further development of foreign trade and investment cooperation.

Among the Republic's leading commercial partners-, one should mention a number of industrialized nations, such as the US, Austria, Belgium, the UK, Germany, the Netherlands, Italy, France and other EU member states, as well as

Korea, Japan, Turkey, Israel, India and. China — in Asia, and Russia, Ukraine and Kazakhstan -in the CIS.

For the time being, the Republic of Uzbekistan is involved in the realization of a whole series of projects, both investment and commercial, together with trading partners from these countries, with active participation of international financial institutions, including the World Bank, the International Monetary Fund, the European Bank for Reconstruction and Development, the Asian Development Bank etc. One of the directions of Uzbekistan's foreign trade policy is activation and further intensification of its commercial and economic linkages with Central Asian states. The established free trade regime proves to be an effective mechanism for raising the level of reciprocal trade within the region[116].

As is known, in the course of the Summit of the Council of Heads of the OCAC member states, held in Astana (Kazakhstan) on May 28, 2004, the President Islam Karimov of the Republic of Uzbekistan has come out with an initiative to create a common market in Central Asia on the basis of the step-by-step progression of economic integration processes taking account of the interests and specificity of economic development of each of trite region's republics. The creation of the common market stipulates not only the introduction of the free trade regime between the countries, but also the unrestricted movement of labor resources and capital within Central Asia.

This initiative is extremely,; important not only for the republics of Central Asia, but also for their foreign trading partners, since the common market will increase both the inflow of overseas investments to the region and the level of trade in goods and services. A wide support of a given initiative in the political and economic "circles testifies to its singular importance for Central Asia.

With this initiative in view, the US Government and the Governments of Kazakhstan, Uzbekistan, Kyrgyzstan, Tajikistan and Turkmenistan have signed

[116] ibid

the Agreement on the development of relations in the field of trade and investment. At the sitting of the Council of Heads of the OCAO member states, a decision has been made to work out a concept, on whose basis to develop the Central Asian common market. The initiative envisages the participation of Afghanistan in the process as an essential element of integration within the region. Additionally the sitting participants have approved Conventions on the creation of water-and-power, transport and food consortia, which are expected to ensure the effective use of the region's waters and-power, transport and food potentialities.

In the first 3 quarters of the current year, foreign trade, turnover of the Republic of Uzbekistan with the Central Asian countries has amounted to some US $500 million, an increase of 34 per cent over the same period a year ago. At the same time, exports in this period have reached US $268.4 million, imports — US $203.8 million and the positive turnover balance -t US $64.6 million[117].

THE PROCESS OF THE REPUBLIC OF UZBEKISTAN ACCESSION TO WTO: EXPERIENCED OF PAST STAGES

WTO accession procedure is prescribed by the Article 12 of the Marrakech Agreement on "WTO establishment" In practice, accession procedure demand long-term and complicated negotiations of four stages:

- Stage of Formalities and Memorandum; submitting of application for accession to WTO and Memorandum on a country –applicant trade regime;
- The Stage of Questions and Answers: WTO members study and assess Memorandum viewing the country-applicant trade policy aspects;
- The Stage of Multilateral and Bilateral Negotiations: negotiations between the country applicant and countries-WTO members in regard of terms and time for the county applicant to access WTO. This stage covers both multilateral negotiations between the country-applicant and specially formed WTO

[117] ibid

working group, and bilateral negotiations of this country with WTO members that have the most apparent trade interests in the country-applicant;

- Conclusion of legal act on accession- ratification of accession act thus putting the act in effect .The period of accession to WTO may last for long years. Negotiations on country accession to WTO may go on until parties come to agreement. And concrete meaning of “agreement terms” is the subject of negotiations between countries -WTO members and a country –applicant. The negotiation process on accession of any country to WTO is characterized by the narrowness of negotiations: the country-applicant must demonstrate to the WTO members how it is going to meet the WTO existing requirements, provided that it cannot change them. WTO members may demand that the country-applicant should reduce the extent of protectionism at the national market, but the country –applicant cannot expect the same from WTO members. The first stage of accession to WTO is the submission of application and memorandum on a country trade regime. After the country-applicant has sent its letter-application to the WTO Director- General declaring intentions to access WTO, the WTO General Council, upon presentation of the Director - General initiates the consideration of the official application. The General Council is composed of the representatives of all WTO members. The General Council forms the working group and its chairman. This group will begin and conduct negotiations with the new candidate seeking accession to WTO in conformity with technical tasks. All countries- WTO members can be included into the Working Group, but usually this group is composed of the countries that have trade links with the country-applicant and the most active participants, i.e. USA, EU, Australia and Japan. Presentation of the full and comprehensive memorandum on the trade regime is the first important step to accession to WTO. The Memorandum on the trade regime is a document, that characterizes and describes in details measures and institutions involved in the country-applicant foreign trade practice.[118] The Memorandum, as a rule, touches upon problems that do not concern only trade of commodities and services-although the latter anticipates financial sector, insurance, telecommunications, professional services, and others -that, by themselves, is a huge work, but also various aspects of macroeconomic policy, particularly in terms of exchange rate regulation, antimonopoly policy, protection of intellectual property and privatization of enterprises. Having presented the Memorandum on the trade regime the country receives the WTO Associated Member Status. As soon as the Memorandum is sent to the Working Group members the WTO accession process enters the next, important stage –the state of questions and answers. This stage requires the longest period. The first part of this process is dedicated to first priority questions and answers on measures and institutions regulating foreign trade and mentioned in the Memorandum on trade regime. The first part of this period ends at the moment of the first personal meeting between the Working Group and the country-applicant delegation. Resulting from discussions and approval received during the Working Group/Country Delegation meeting the new, more specific questions on trade policy measures and its regulation by the country-applicant are asked. Regular meetings in order to work out the common position on terms allowing the country applicant to access WTO may take the long period. They may not concentrate only on study of Memorandum. Upon completion of the "question/answer" stage the country –candidate presents to the Working Group its initial program of "suggestions" on access to the market. Thus, the accession process enters the third stage of bilateral negotiations between the country-candidate and each country- WTO member wishing to discuss the accession terms expressed through level of tariffs, access to market of services and etc. When bilateral negotiations reach their logical conclusion and the

118 ibid

Working Group is convinced that the legal and institutional basis of the country-candidate conforms to the WTO requirements and norms the Secretariat presents to the Working Group the draft report determining the country-candidate accession procedure. Upon Working Group approval this report goes to the General Council. Following the positive decision of the General Council the county-candidate is invited to sign the Protocol on Accession to WTO. In December 1994 the application of intention to access WTO in the Full-Fledged Member Status was sent to WTO on behalf of the Government of the Republic of Uzbekistan. The application received positive respond and the Working Group had been formed to direct Uzbekistan accession to WTO. In September 1998 the presentation of Memorandum on Uzbekistan foreign trade regime was organized in WTO. Written answers to questions asked by a number of countries-WTO members were prepared and sent to Secretariat of this organization. In December 1998 the Government made a decision[119], according to which the staff of Inter departmental Commission to work with WTO had been approved. Representatives of the Agency on Foreign Economic Relations, the Ministry of Macroeconomics and Statistics, Ministry of Finance, the State Tax Committee, other ministries and departments were included in the Commission. According to the Decree, the Agency on Foreign Economic Relations was entrusted functions of Secretariat of Inter departmental Commission. A number of Commission meetings had been held. Official delegations from the Republic of Uzbekistan took part in three WTO Ministerial Conferences held in Singapore (1996), Geneva (1998) and in Seattle (1999). Within the second stage of accession to WTO working groups were formed in ministries and departments on:

- Preparation of information on sanitary and phytosanitary measures and technical barriers in trade;

[119] Decree of the Cabinet of Ministers of the Republic of Uzbekistan# 520 of 14.12.98

- Preparation of information on internal support and export subsidies in agriculture;
- Preparation of information on measures in policy concerning trade of services;
- Preparation of information within the WTO agreement framework on trade aspects of intellectual property tights;
- Preparation of suggestions on tariff concessions for commodities and liabilities on services;
- Making alterations to the national legislation according to WTO agreement provisions;
- Preparation of research on assessment of the impact made by Uzbekistan accession to WTO on various economic sectors.

On July, 17, 2002 the first Working Group meeting on Uzbekistan accession to WTO was held in Geneva. The main issue of agenda was article -by-article study of the memorandum on foreign trade regime in the Republic of Uzbekistan. During discussion the most active and interested in discussion of foreign trade policy measures in Uzbekistan were representatives of delegations from USA, EU, Switzerland, Korea and Australia. The questions covered such areas as price regulation, regime of access to foreign currency, regulation of access to Uzbekistan market of commodities and services, existing restrictions in this sphere, custom tariff level, plan for application of Harmonized System, 2002, customs payments and methods of their levy, regime for import of goods from CIS countries. As for the protection of intellectual property rights it was recommended to apply in practice the country legislation in this sphere and join Bern's Convention. Current phase of accession to WTO is characterized by the implementation of works that help to resolve the broad range of organizational, legislative, technical and other issues relevant to the preparation for the oncoming meetings of the Working Group. So, the country has passed the preliminary stages of accession to WTO and now it will have to begin negotiating with countries -

WTO members. This process may require concentration of considerable resources and make clear definition of the country position on debatable issues mentioned below. A part of the questions may be accepted and has already been accepted due to implemented reforms. The work carried out earlier revealed that the country legislation relevant to the sphere and scrutinized in the report is in the process of permanent development. It is apparent from the character of answers on the Memorandum and on the content of the Memorandum that the government directed to countries-members. If, answering the questions of US Government, our side focused on convertibitility, licensing of foreign trade activity, in answers to additional questions we gave explanation of alterations in legislation that considerably improved aspects under discussion.[120] As it was noted before, the Memorandum became obsolete and requires permanent updating. Still, there is a number of problems mentioned practically by all countries-WTO members. It stresses the need for further implementation of measures that help to bring the national legislation in conformity with provisions of WTO agreements.

New negotiations agenda toward to WTO

Formation and improvement of the republican foreign trade regime is closely linked to social economic development of the country. Many-facet aspects of social –economic policy plunge the country into the depth of protectionism, first, but, second, globalization challenges determine the economic growth potential to integrate into the world market. But in any case, building of feasible and adequate policy on protectionism and liberalism must be based on pragmatic approaches that take into account international practice and principles of law. [121]Improvement of legal base of foreign trade relations as well as creation of more flexible trade regime adequate to requirements and real situation in economy development may

[120] Muradova Kh.,Khusnia@cer.uzAbdurazakov A .Uzbekistan, Center for Economic Research, Ref.#1188, N72 -Selected Papers "Foreign Trade Regime of Uzbekistan and Its Compliance to Norms of Agreements of WTO" Available at www.gtap.agecon.purdue.edu/resources/download/1834pdf

[121] ibid

be achieved only through legal system adjusted to basic norms of international trade laws, where the World Trade Organizations serves as the guarantor of such a law in current globalizing environment of International trade. This report is the first one dedicated to the legal aspects of Uzbekistan accession to WTO. Therefore, the work on assessment of perspectives for Uzbekistan accession to WTO had started from comparison of trade regime regulation of Uzbekistan and WTO basic principles. The conducted analysis on existing trade regime in Uzbekistan and the extent of its compatibility with WTO requirements allows to make the following conclusions and recommendations:

- Rather simplified and flexible regime on regulation of commodity trade does exist in Uzbekistan. Particularly, the practice on application of quality import/export quotas prohibited by the WTO rules is not used, the types of import contracts due to be registered in the Agency for Foreign Economic Relations have been curtailed and real conditions are being created for further cutting down of such a list. It indicates the further trade liberalization in Uzbekistan. Yet, regulation of import goods needs to be brought to terms of WTO practice on internal taxation and import duties. In this case the methodic on tax estimation and levy and the area of their application must precisely fit into the national regime. The great job must be done in order to improve the use of technical barriers in trade, i.e. reformation of standardization and certification systems. As for export regulation, according to WTO requirements, it is necessary to continue narrowing the list of commodities banned for export. This measure may create additional pre-requisites for the growth of country export potential. In the result of elimination of misbalance between the internal and external prices the need for licensing of non-strategic commodity must be no longer relevant. Still, the most significant problem in this aspect will be the harmonization of norm in the sphere of export subsidizing and support to national import substituting production and sectors. Therefore, it is necessary to receive the "developing country" status in the process of negotiations on accession to WTO. It will allow retaining some volume of medium -term support to perspective sectors.

- As for regulation of trade of services there are no significant restrictions. The trade of services is not the subject of the Law "On foreign economic activity", Custom Code and other acts. Due to their specific character and their diversity, they are regulated in the current time by the special laws, for example, the Law "On insurance activity" and sub departmental acts which cover some services. In the context of negotiations with WTO the sphere of services will occupy the special place for industrially developed countries. Therefore, the development of common policy in this area will be necessary taking into consideration that the sphere of services will include such most important economic spheres as banking business, insurance, business services, telecommunications, transport, tourism and etc.
- Uzbekistan has developed required legal base for protection of intellectual Property. In future, procedures on intellectual right protection should be set forth clearly to eliminate violations in this area. It concerns, first of all, administrative and criminal legislation and relevant legal procedures and frontier control system. Considering the economic importance of property protection great attention, upon Legislation improvement should be paid to responsibility for breach of intellectual property rights. Besides, within the accession to WTO, the republic will have to join Bern and Rome conventions on intellectual property right protection.
- For transit regulation Uzbekistan practices differential regime. WTO agreement system creates favorable conditions for cargo transit through the territories of countries-WTO members. At the same time Uzbekistan, with very convenient geographical location, may serve as the center of transport corridors going through Central Asia. For this purpose the good incentive

may be unification and optimal reduction of transit duties regardless of country of destination and transit cargo origin.

- Considerable disproportion of internal and external prices for agricultural goods exists in agriculture regulation system that requires reformation of competitive environment in agriculture and minimization of sate order role price formation system. Main direction of reformation is creation of for specific goods.
- As for institutional aspects of Uzbekistan accession to WTO it is worth establishing a permanent body and staffs it with specialists from relevant ministries and departments. The objective of this approach is to invite experts on all spheres of WTO regulation and deal with problems of accession at the professional level. The important aspect is also the guaranteeing the professional level and permanent character activity of members of Uzbekistan delegation conducting negotiations on accession. It is required by the fact that negotiations take a long time; require Professional and logical position of the country in settlement of all problems of accession both normative and organizational.

The Republic of Uzbekistan has been making persistent effort to liberalize its foreign trade sector .Liberalization is not an end in itself rather it serves as one of the vital instruments of nations economic policy. A positive dynamics in the amount of foreign turnover witnessed in Uzbekistan during 2003 and 2004 bears the evidence upsurge in the country's economic development.

About the choice between regionalism and multilateralism in trade relations, the Central Asia economies clearly opted for the multilateral option. Regionalism though appeared attractive, but on deeper thinking preferential regional trading arrangements are unattractive. Multilateralism in the form of

WTO membership looks like an unattractive restriction on policy autonomy, but on deeper analysis it is the best framework that the Central Asian countries can have to develop their international trade relation. Thus WTO membership appears to be a natural institutional counterpart to economic openness. However the Central Asian countries in their initial phase were highly suspicious of the international obligations that place constraints on their policy autonomy. They joined the United Nations as a signal of nationhood, and the IMF and World Bank and the regional development banks as potential sources of capital. Apart from the Kyrgyz Republic they held back on WTO accession. For Turkmenistan, this attitude is still continuing as the President views WTO membership as incompatible with the country's policy autonomy and neutrality.

In export performance Kazakhstan and Uzbekistan have relatively superior position in the mid-1990s partly because of the favorable energy and cotton prices and their divergent experience after 1997 and partly by because of the drop in world cotton prices since 1996 and booming oil prices since 1999. Over half of the Central Asian countries' international trade is with the non-CIS countries, the lead being taken by Uzbekistan. It reflects primarily the ability of Uzbekistan to sell cotton in the world market.

Among the Central Asian economies Kazakhstan, was slow to diversify its markets, because of the reliance on oil pipelines and mineral-processing links and its proximity to Russia, the CIS share of Kazakhstan's trade has fallen to half in 1997 and dropped substantially further in 1999 during the export boom following devaluation of the currency. Only Tajikistan is significantly dependent on CIS suppliers, and this is due to its geopolitical and military considerations as unrequited imports are provided by Russia and Uzbekistan

In sum, with all the reservations noted in this chapter the Central Asian countries are open economies. The two countries with the most restrictive barriers to trade are Turkmenistan and Uzbekistan. They are necessarily trading nations as they have comparative advantages in natural gas and in cotton. The Kyrgyz

Republic and Tajikistan are open in terms of low trade barriers, but the volume of their international trade is limited by its relative resource scarcity and by their landlocked status and which causes difficulty of transiting for the neighbors. Kazakhstan is the biggest trading nation, with the highest world oil prices.

The Central Asian economies in their process of economic reform met with varying degree of success based on their existing infrastructure, political, social, and economic conditionalities, and the willingness and initiative of the government of the day. The present trade policies reflect the fact that all the five republics intend to liberalize their respective economies and integrate with global economy. In this attempt Kyrgyzstan has taken the farthest step, to joining the WTO and it is making its trade policy in compliance with the WTO rules and regulation. Kazakhstan and Uzbekistan are under observer status and they consider accession to WTO as one of the major priority. In relatively short period of time, Kazakhstan has been remarkably successful in its effort to gain access to world market. Uzbekistan is consistently pursuing the "open door" policy in the external trade domain. The foundation was laid down at the initial stage of economic reform, the trade policies aims to ensure the maximum development of foreign trade and investment cooperation. As for Tajikistan the country aims to deepen the integration of its national economy into the world economy. In this context, one of the key issues of the external economic policy of Tajikistan for the nearest future will be accession to the WTO. At present Tajikistan's foreign trade policy is oriented towards development of the export potential of the country. For Turkmenistan, although it was slow to begin with the process of economic reforms, it is trying to diversify its export and liberalize its economy in order to meet the challenges of the changing global order.

CHAPTER – 4

CONCLUSION

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Trade among societies and countries has been continuing since historical period. The main reason behind foreign trade is to promote welfare by exchanging of those goods which can't be produced domestically or cannot be produced at cheap prices in that country. Foreign Trade has been a critical area of study by Economists. Various theories of international trade have been put forward and they favor international trade as a means to promote economic growth.

Main theories which contend that international trade is favorable to economic growth and development are Theory of Absolute Advantage of Adam Smith, Theory of Comparative Advantage of David Ricardo, Theory of Factor proportion hypothesis or Heckscher-Ohlin theorem and Product Cycle Theory and many others.

Some of the Modern theories of trade have criticized International Trade on The grounds of promoting inequality and favoring the rich nations at the cost of the poor nations for example Dependency theory. However in spite of these criticism positive aspects of the international trade cannot be relegated to backburner. We need to correct the negative impact of international trade on domestic economy and redistribute the benefits of the trade to minimize economic inequality, with appropriate policy. International trade has helped economic growth in some developing countries but at the cost of agriculture and rural development. It has not helped in broad-based economic and social development. The citizen of an economy which depends greatly on international trade will benefit only when the government has a policy to spread the benefits of the trade.

The gains from international trade are of little benefit to most of the people in a developing country unless accompanied by appropriate domestic reforms.

Trade Expansion and Inclusiveness of the economic growth process, it is important to note the link between trade liberalization, economic growth and poverty. Since expansion of trade is possible only through liberalization which in return will encourage growth and the economic growth can reduce the extent of poverty. The widely-accepted view among economists is that, with other things the same, Countries with few restrictions on trade will have faster economic growth than countries that heavily restrict trade, and that absolute poverty will be reduced more quickly with faster economic growth. It follows that countries are encouraged to reduce trade barriers in order to reduce absolute poverty. Trade liberalization is seen as leading to faster economic growth because it reduces distortions in price relativities and allows those activities with a comparative advantage to develop. Poor countries usually have high ratios of labour to land and labour to capital and thus have a comparative advantage in labour-intensive activities. Development of labour-intensive activities in these countries provides income-generating employment for larger numbers of poor people than trade - restricting policies that distort relative prices in favor of capital-intensive activities. There is debate over the benefits of trade liberalization for poverty reduction. Differences exist over the impact of trade liberalization on economic growth and over the relationship between economic growth and reductions in poverty. It is contended that a trade liberalization strategy should not be thought of as a policy to reduce absolute poverty. Rather, trade liberalization strategies should be designed so as to achieve trade liberalization in the most effective way and to minimize adjustment costs. The poverty reduction strategy should be separate and should focus on identifying and removing obstacles to the poor participating in economic activities. In this way the impact of trade liberalization on economic growth and the reduction of absolute poverty as the result of growth should both be maximized. In these terms the importance of international trade has been argued in the first chapter.

The central Asian countries of Kazakhstan, Kyrgyzstan and Uzbekistan, Turkmenistan and Tajikistan emerged as independent state after the disintegration of the USSR and are among the eleven former Soviet republics which formed the commonwealth of independent states. The five Central Asian economic countries are undergoing economic transition .They are moving from central planned economy to a market economy, towards liberalization, globalization and privatization. Under the centralized planning systems central Asian states had highly specialized and closely integrated economic relations with the rest of Soviet Union. It was characterized by strong dependency on imports of energy, food and consumer good. The production structure was oriented towards agriculture and mineral extradition thus there was very little growth of import substituting industries. The export base of the central Asian states had very minimum degree of diversification and import dependency was high which made these economies vulnerable to adverse trade shocks. Following independence the central Asian states (with the exception of Turkmenistan until 1997) continued to incur sizeable and persistent external current account deficits. Three main factors accounted for this first, the agricultural, industrial, and household sectors inherited from the Soviet Era was highly energy intensive. Second the demand for investment goods to replaced obsolete capital was high. Third after the years of repressed consumption import demand for western consumer good was very high. Hence import from non-traditional markets grew rapidly in spite of the attempts made to restrain imports through foreign exchange restrictions.

The Central Asian economies inherited state-controlled foreign trade systems from the Soviet era, where foreign trade was subordinated to the requirements of the central plan. Exchange rates were administratively determined under a complex system of multiple currency practices. The management of foreign economic relations lacked transparency, with responsibility shared among several organizations including the planning agency (Gosplan), the state foreign economic commission, the ministry of foreign economic relations and other specialized foreign trade organizations. The opportunity or incentive for individual enterprises to engage in foreign trade was very limited.

For this transition they are faced with policy dilemmas like the choice between the Regionalism and Multilateralism. In addition to this they face many obstacles in the path of liberalizing and deregulating the external sector. Domestic political condition, authoritarian regime, ethnic disputes, problem of law and order etc are serious hindrance in the path of deregulating and liberalizing the foreign trade. They faced large macro economic imbalance at the time of independence as transactions within the erstwhile USSR were based on the Central Pan and implemented through mandatory production and delivery targets. These economies have now embarked on the path of economic reforms. As their economies are stabilizing they are becoming more integrated with rest of the world. The Central Asian states comprising of Kazakhstan, Kyrgyzstan, Tajikistan, Turkmenistan and Uzbekistan are rich in natural resources. This region is abundant with minerals, especially hydrocarbon resource. These states are newly independent and were part of Soviet Union. They were not only politically integrated with USSR but were also economically integrated with the political separation countries need to separate on economic lines. They are organizing their economies on their own. They have established their own central banks, currencies and other economic and financial institution. This also hold true in the field of trade also. The Central Asian countries are conducting their foreign trade with increasing openness and confidence. These countries are widening the space of cooperation by collaborating with multinationals and others to enhance the pace and progress of their economic development. This policy have resulted in the arrival of host of multinationals in energy and other sectors of these economies and Central Asia has become one of the focal point of global economic interests. The Central Asian states have unlimited growth potential. Once the natural resources especially hydrocarbon resources from these Central Asian states reach the international market, the potential of growth in these economies in very high.

The growing markets in these Central Asian countries are reported to have the potential of becoming one like the gulf countries. Therefore the Central Asian states that are going through the period of economic transition have very bright future prospects owing to the abundance of its natural resources. In this period of transition the centralizing states faces the dilemma of regionalism vs. multilateralism, this has been the major issue for all the Central Asian states. With the passage of time and the growing experience they have reached a clear cut, solution, for the choice between regionalism and multilateralism in trade relations, the Central Asia economies clearly opted for the multilateral option. Regionalism though appeared attractive, but on deeper thinking preferential regional trading arrangements are unattractive. Multilateralism in the form of WTO membership looks like an unattractive restriction on policy autonomy, but on deeper analysis it is the best framework that the Central Asian countries can have to develop their international trade relation.

The progress towards trade liberalization has varied in degree across the Central Asian states. The roles of the state in foreign trade have been significantly reduced. The degree of progress is high in Kazakhstan, Kyrgyz republic and Tajikistan. The highly restrictive state monopolies on foreign trade have been eliminated; licensing requirement relaxed and significant tariff reforms has been initiated. The progress towards liberalization is more gradual in Turkmenistan and Uzbekistan, where state continues to play a dominant role, particularly in the foreign exchange market.

The central Asian sates have benefited from world trade that is by liberalizing its economies and trying to integrate itself with the world economy through its increase in foreign trade. Exports have grown significantly and the regions have been broadly successful in diversifying markets. The movement towards world prices has on the whole benefits the region. The general tendency of the Central Asian economies is that they are moving towards multilateralism in order to get more avenues of foreign trade. All the Central Asian countries have shown their desire and willingness to join the WTO as they are of the view that such membership shall eventually bring economic benefits for these countries. But the conditions and requirement of WTO membership pose a particular problem for these countries. The economic structure, economic regulations and economic policies of these countries are not in tune with the conditionalities, rules and regulations framed by the WTO for countries to adhere in order to become its members. The most important benefit of WTO membership would be to place all Central Asian trade on a common basis of international trade law, and potentially to separate trade from politics.

In terms of Foreign Trade the Central Asian economies differ in their trade structure as well as the trade policies, based on their initial condition and geographical factors and other related factors. Recently the entire trade structure stands under transformation because of the disintegration of the former Soviet Union. Central Asian economies in their process of economic reform have taken globalization as their goal therefore they are going for liberalization of their respective economies. Therefore they are relying more on market forces which is a shift from the state controlled central planning economy. As a part of the globalization policy, export promotion has gained more and more importance and the merits of import substitution have reduced in importance. These republics have been making or intend to make efforts to restructure foreign trade policy and boost their foreign trade.

The economies differ in their trade structure as well as the trade policies, based on their initial condition and geographical factors and other related factors. Recently the entire trade structure stands under transformation because of the disintegration of the former Soviet Union. Despite many proposals for regional trading arrangements, in practice the Central Asian countries have in their trade policies clearly chosen the path of policy autonomy combined with non-discriminatory multilateralism. Foreign trade structure and trade regime of five

Central Asian countries are similar in some aspects but differ from each other on many aspects due to diverse political, historical, geographical and social condition.

All Five Central Asian countries have shown willingness to restructure their foreign trade policies and liberalize their economies keeping in tandem with the era of globalization. They have come out of the regulated centrally planned soviet era economy and are making efforts to diversify and open their economy for increased foreign trade. In export performance Kazakhstan and Uzbekistan have relatively superior position in the mid-1990s partly because of the favorable energy and cotton prices and their divergent experience after 1997 and partly by because of the drop in world cotton prices since 1996 and booming oil prices since 1999. Over half of the Central Asian countries' international trade is with the non-CIS countries, the lead being taken by Uzbekistan. It reflects primarily the ability of Uzbekistan to sell cotton in the world market.

Among the Central Asian economies Kazakhstan, was slow to diversify its markets, because of the reliance on oil pipelines and mineral-processing links and its proximity to Russia, the CIS share of Kazakhstan's trade has fallen to half in 1997 and dropped substantially further in 1999 during the export boom following devaluation of the currency. Only Tajikistan is significantly dependent on CIS suppliers, and this is due to its geopolitical and military considerations as unrequited imports are provided by Russia and Uzbekistan

In sum, with all the reservations noted in the third chapter the Central Asian countries are open economies. The two countries with the most restrictive barriers to trade are Turkmenistan and Uzbekistan. They are necessarily trading nations as they have comparative advantages in natural gas and in cotton. The Kyrgyz Republic and Tajikistan are open in terms of low trade barriers, but the volume of their international trade is limited by its relative resource scarcity and by their landlocked status and which causes difficulty of transiting for the neighbors. Kazakhstan is the biggest trading nation, with the highest world oil prices.

The Central Asian economies in their process of economic reform met with varying degree of success based on their existing infrastructure, political, social, and economic conditionalities, and the willingness and initiative of the government of the day. The present trade policies reflect the fact that all the five republics intend to liberalize their respective economies and integrate with global economy. In this attempt Kyrgyzstan has taken the farthest step, to joining the WTO and it is making its trade policy in compliance with the WTO rules and regulation. Kazakhstan and Uzbekistan are under observer status and they consider accession to WTO as one of the major priority. In relatively short period of time, Kazakhstan has been remarkably successful in its effort to gain access to world market. Uzbekistan is consistently pursuing the "open door" policy in the external trade domain. The foundation was laid down at the initial stage of economic reform, the trade policies aims to ensure the maximum development of foreign trade and investment cooperation. As for Tajikistan the country aims to deepen the integration of its national economy into the world economy. In this context, one of the key issues of the external economic policy of Tajikistan for the nearest future will be accession to the WTO. At present Tajikistan's foreign trade policy is oriented towards development of the export potential of the country. For Turkmenistan, although it was slow to begin with the process of economic reforms, it is trying to diversify its export and liberalize its economy in order to meet the challenges of the changing global order.

Each of the Central Asian economies have different story of success and failures. It's difficult to draw comparison between them because each of the country is faced with different political, economic, social and geographical condition. Moreover political willingness to carry out trade reforms and ideological context also played an important role in determining the success of trade reforms. However it is clear from the above discussion that is process of restructuring of the old economy and carrying out the economic reforms in order to meet the challenges of independence and the existing global order is neither simple nor an easy task. It is a complex as well a difficult process. Still Central Asian countries have to do much to liberalize and diversify their economies to boost foreign trade as they are still minor players in global market. There economic condition is still weak in terms of foreign trade.

These five Central Asian countries should follow appropriate policies to diversify their economy, strengthen their linkages with neighboring as well as with other global players to boost their economy. They should maintain law and order condition to boost foreign direct investment, import of technology and cooperate with their neighbors to establish strong economic union where trade can flourish unabated. They should try to democratize their political system as this would give them global acceptance as trading partner. They should also try to mould there way according to the rules of WTO to access the membership of WTO. This would certainly benefit them in terms of expanding foreign trade, as it will provide them access to more markets without any discrimination. These, five Central Asian countries have the potential to increase their foreign trade but still challenges are ahead, and it all depends on the success of each country in reforming and restructuring their economy. The most important part of the challenges of globalization is how the political and economic leadership handles the issues. The success of the trade reform depends much on the government initiative and adoption of appropriate policy measures. This is so because trade requires sound institution and sound infrastructure and simple transparent procedures. Bureaucratic, institutional and infrastructural constraint of trade has to be addressed before trade can expand and the countries can reap substantial economic benefit. In case of many less developed economies trade has promoted economic growth when accompanied by appropriate policy measures. Thus with the required set of polices and government action Central Asian economies can also have "trade led growth". For this the government along with the trade liberalizing measures has to pursue appropriate policy measures of income redistribution such that the benefits of trade are not corned by a small segment of society. This approach can only establish the link between trade liberalization, economic growth and poverty. Trade liberalization policies depend on the market forces. Free trade is possible under free market rules and lack of Government intervention .Trade is said to promote economic welfare of the trading nations, in many countries it is seen that trade has promoted economic inequality instead of economic growth when it is not accompanied by appropriate domestic policy measures. Here lies the need of government intervention; this cannot be left on market forces. As it will breed inequality and in the long run and this can also retard the growth processes. Thus to make trade truly an engine of growth the Central Asian economies require appropriate domestic as well as external polices.

Thus the future course of action should look into all these dimensions to make trade reform and trade liberalization, a successful story for the Central Asian republic.

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