

# The unfinished reforms in the Caucasus and Central Asia: What Next?

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## Introduction

- Not easy to speak about CCA region as a whole. Different conditions, history, culture, size, endowments, geopolitical conditions...
- Commonalities: landlocked , ethnically fractionalized, Soviet legacy, autocratic past, history of external and/or internal conflict, dangers of spillovers from instability in other countries, danger of resource curse in resource-rich countries.

## Introduction

- CCA might seem to cumulate many disadvantages...
- ... but extremely high upside potential.
- Many very positive changes have been taking place already, and this needs to be better known to the outside world.
- Wealth of natural resources is enormous opportunity if handled well.
- CCA is on the verge of becoming a thriving economic powerhouse, overcoming all the disadvantages inherited from geography and history.

## Some general lessons from transition.

1. The transition is not just about eliminating central planning and free market forces, it is about creating institutions to support development of the market economy, not only the rule of law and protection of property rights but also effective government, low corruption and high state capacity. Early transition failures and the prolonged slump of the nineties were very much related to institutional weaknesses.

## Some general lessons from transition.

2. There is not one set of institutions or only one path of transition. There is a big difference between the economic success of China and Poland, and success in one country cannot necessarily be replicated in other countries.

3. What appears as unfinished reforms are often divergent institutional paths. What is at stake is not whether or not to finish reforms but what institutional model is to be chosen.

## Some general lessons from transition.

4. There is a strong advantage for countries in transition to have a “role model” to aspire to because it gives a) good sense of direction, b) strong benchmarking, c) can improve accountability. Countries in Central Europe had the EU institutions as model and as condition of accession; China had Taiwan, Singapore and Hong Kong, and other East Asian countries. Russia has not had such a role model. CCA countries have choices of possible “role models”: Turkey, Kazakhstan, Abu Dhabi, EU,...

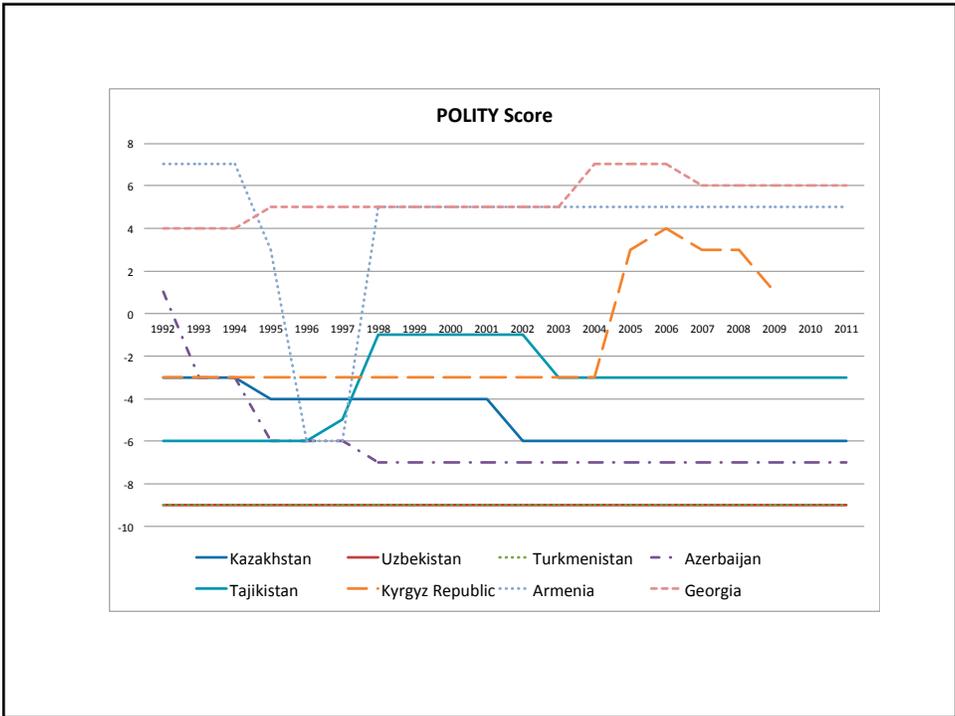
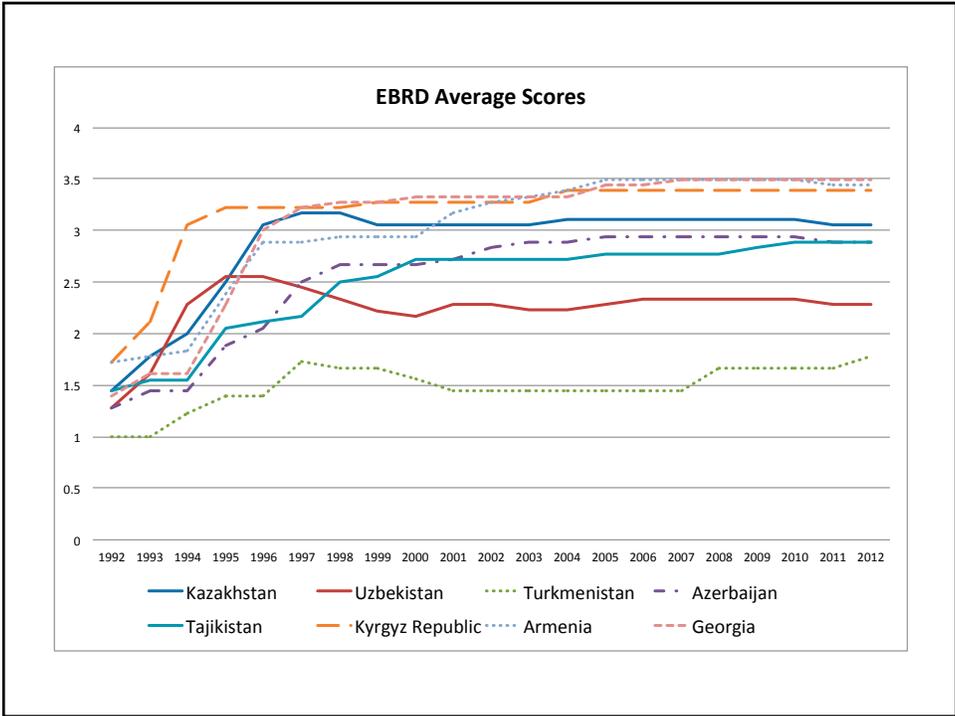
5. Misguided emphasis on privatization of large SOEs relative to entry of competitive SMEs;

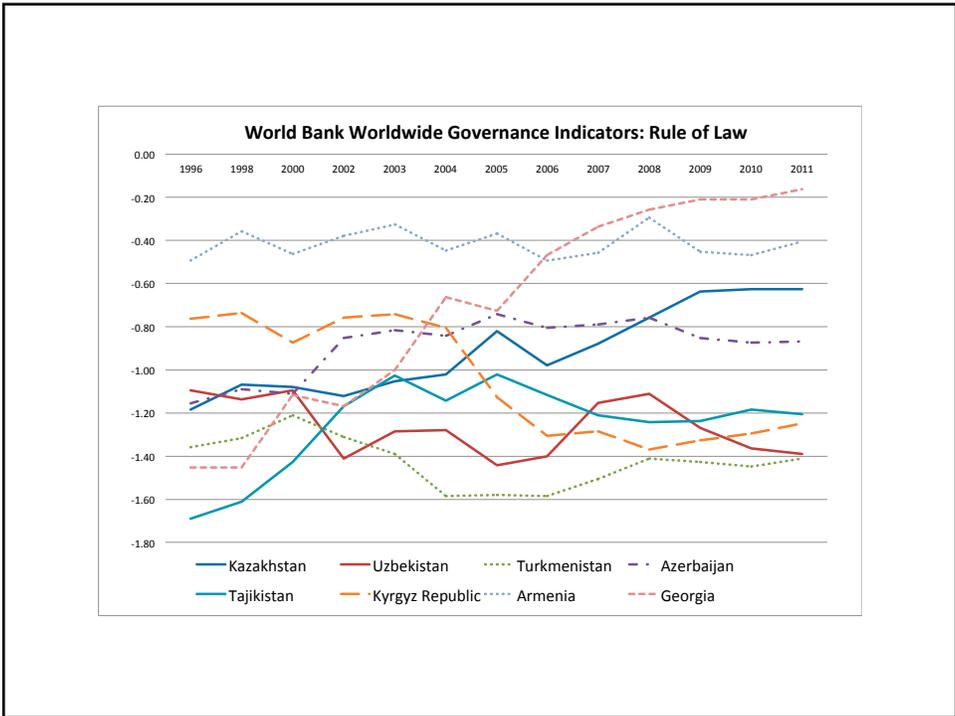
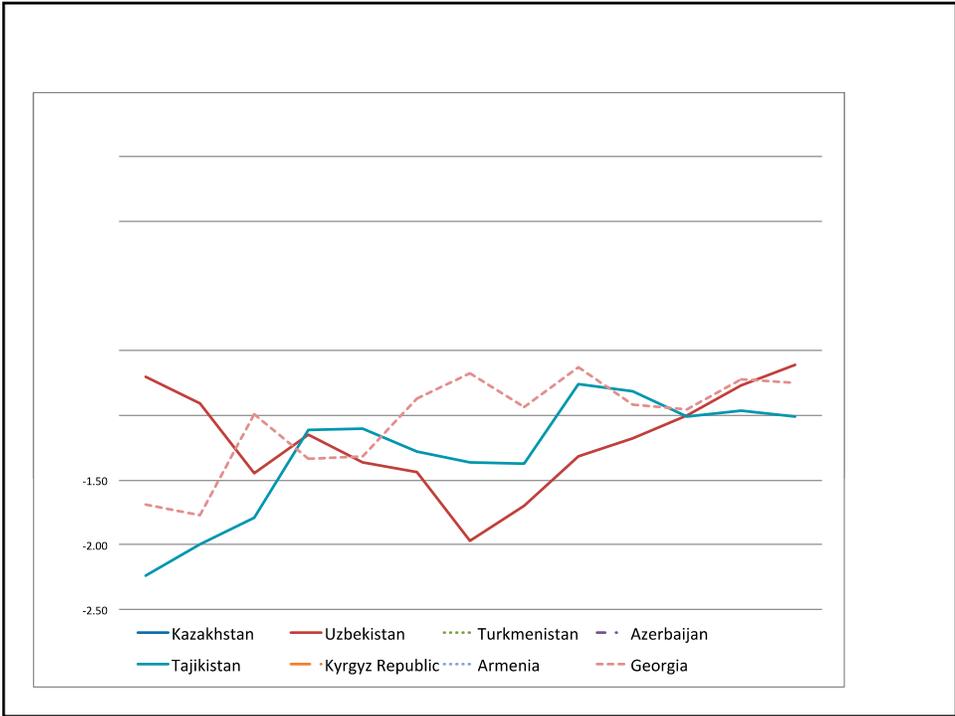
6. Political support for reforms is needed within the population but also within the government administration. Experience of China versus Russia.

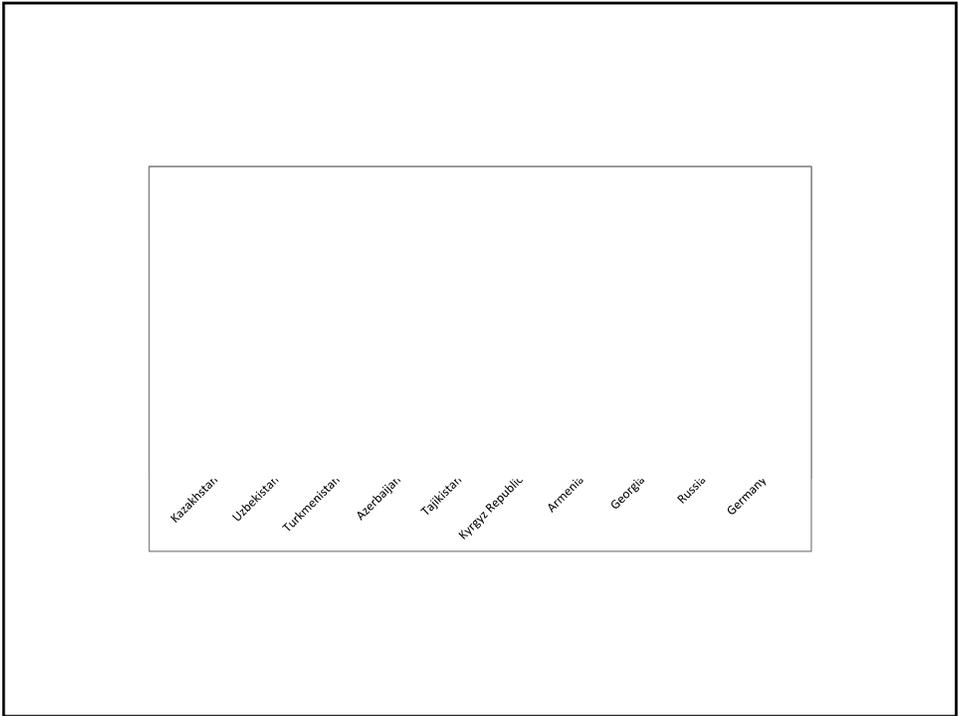
7. Economic openness is fundamental. Participation and competition in world markets is key, but also openness to FDI and technical expertise in all sectors (not just natural resources), without “selling out” natural resource endowment. Openness in education also fundamental for optimal human capital investment.

## Reforms and institutional change in the CCA region

- Reform surge in early nineties but never quite completed. Lower reform effort in Turkmenistan and Uzbekistan.
- No convergence in political institutions. Only Georgia, Armenia and Kyrgyz Republic are recognized as democracies.
- Big variation in political stability, but stability in non democracies often more fragile than it seems.
- Large variation in quality of government.

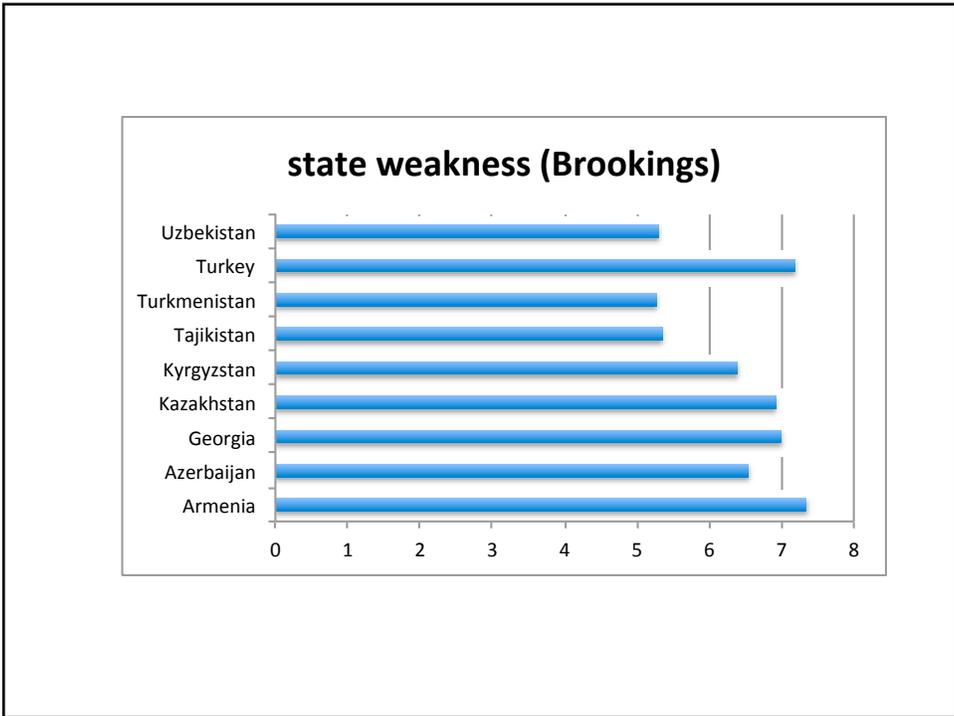
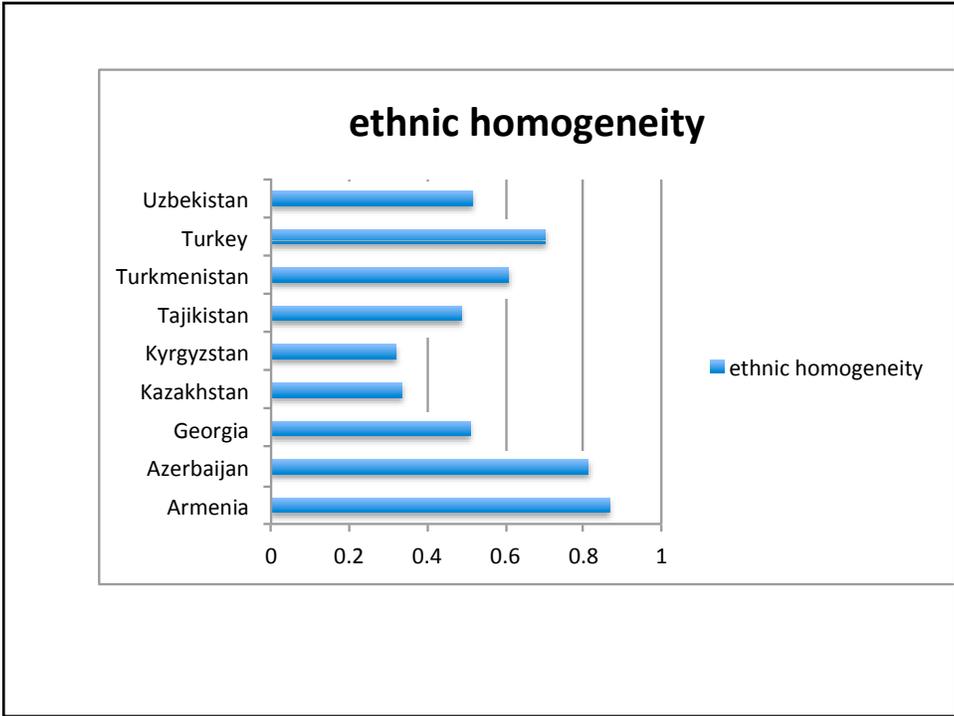


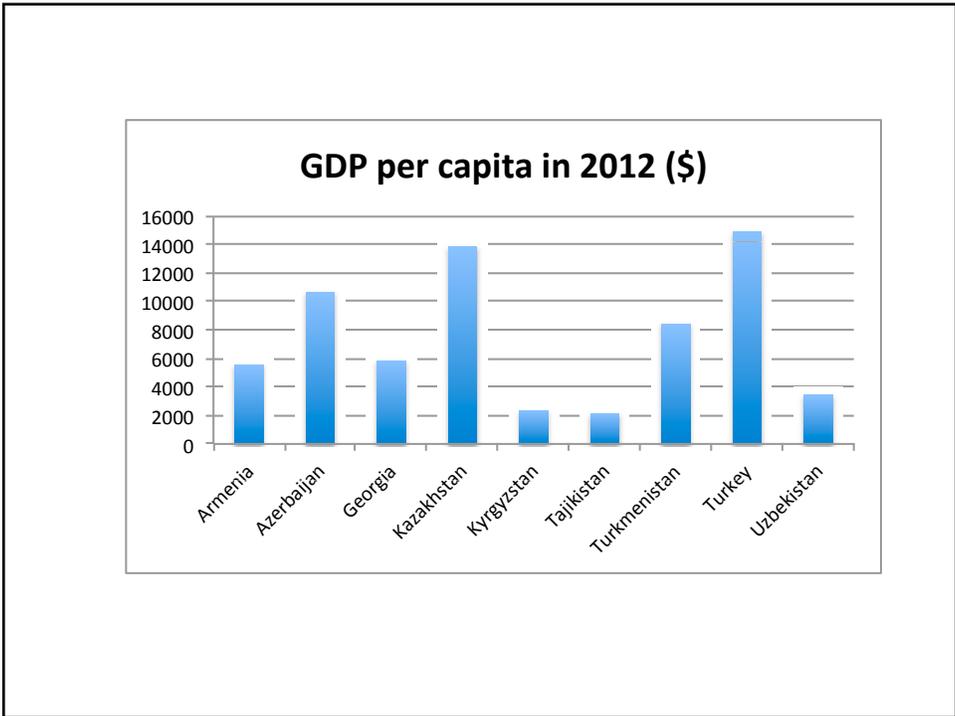
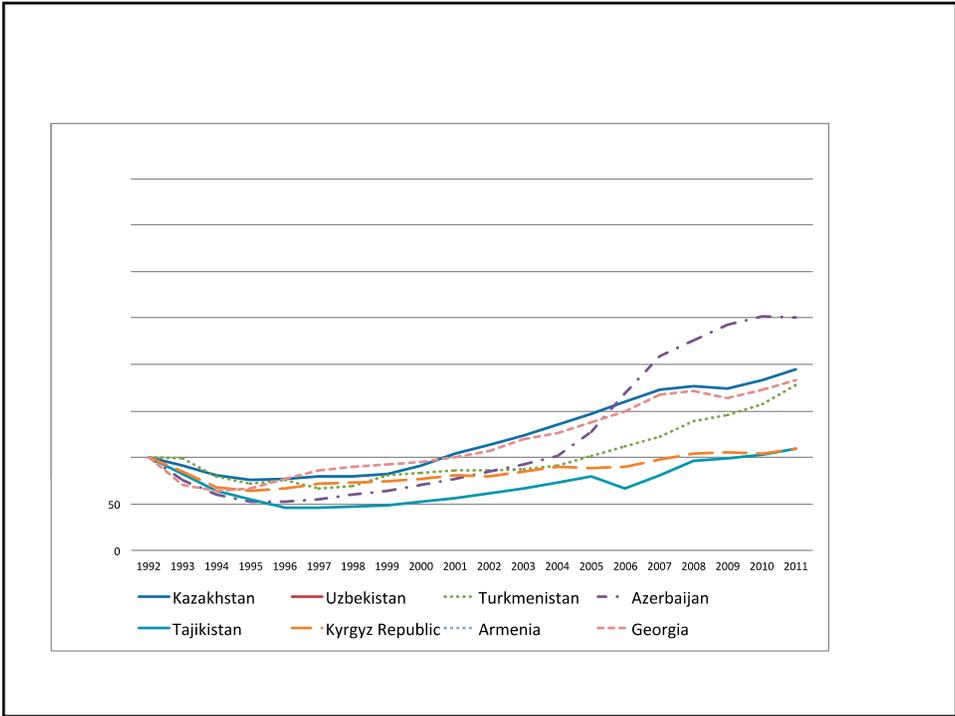


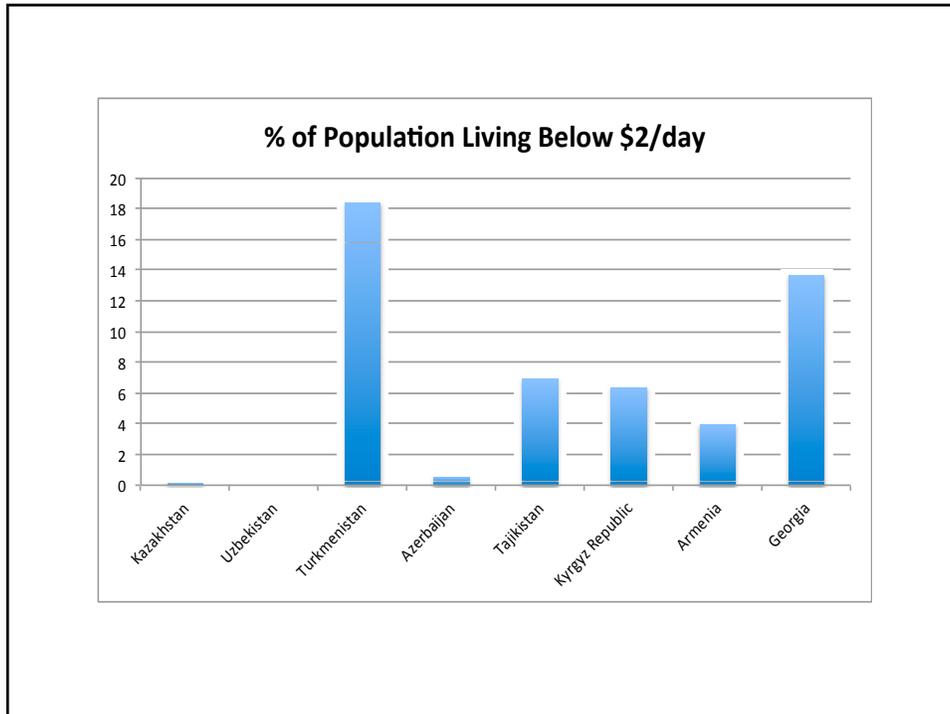


Kazakhstan  
 Uzbekistan  
 Turkmenistan  
 Azerbaijan  
 Tajikistan  
 Kyrgyz Republic  
 Armenia  
 Georgia  
 Russia  
 Germany

2011	2012
Singapore (1)	Singapore (1)
Hong Kong (2)	Hong Kong (2)
Georgia (12)	Georgia (9)
Armenia (50)	Armenia (32)
Kazakhstan (56)	Kazakhstan (49)
Azerbaijan (66)	Azerbaijan (67)
Turkey (68)	Kyrgyz Republic (70)
Kyrgyz Republic (69)	Turkey (71)
China (91)	China (91)
Russia (118)	Russia (112)
Tajikistan (147)	Tajikistan (141)
Uzbekistan (168)	Uzbekistan (154)







## What next?

- CCA shows diverse picture of institutional and economic performance. Countries can learn from each other, on their own initiative.
- What main lessons and recommendations for the future?

## 1. State capacity.

- No successful market economy can emerge without a minimum state capacity and effective governance. There is, however, not necessarily only one way to get there.
- Georgia versus Kazakhstan.
- Georgia was thoroughly corrupt with low state capacity, and implemented impressive anti-corruption campaign.
- Kazakhstan worked at building an efficient government apparatus, productively using oil revenue to diversify, modernize and enhance public good provision. Relative internal peace despite high ethnic fractionalization and openness towards foreign experience and global institutional standard.

## Using the resource rent productively.

- The resource curse is not a fatality. There are positive experiences: Norway, Qatar, Abu Dhabi, Kazakhstan in the region.
- Resource rent can and should be used to diversify and modernize, build infrastructure, education and encourage thriving private sector. Diversification programs are key to economic development.

## Using the resource rent productively.

- Several conditions needed:
  - Internal and external peace
  - Openness to trade, foreign capital, foreign labor (skilled and unskilled), tolerance and respect.
  - Collaboration across the region. Stable and low customs costs, sharing of infrastructure projects (rail, roads, pipelines), learn from each other.
- This might seem naïve but European countries managed to overcome historical enmities to create economic and monetary Union in atmosphere of peace, openness and mobility.

## Conclusion.

- CCA region, despite variable performances, is doing better than the outside world knows.
- Many positive experiences despite the disadvantages of geography and history.
- Resource wealth is not fatality but opportunity.
- Leadership is a key factor. Leaders will either be praised in history for bringing their country to the 21<sup>st</sup> century or blamed for failing to seize the opportunities.