



Central Asia Regional Economic Cooperation Program

MID-TERM REVIEW OF CAREC 2020: A DISCUSSION NOTE

CAREC 2020 Midterm Review: Country Consultations

April–May 2016

Tashkent, Astana, Bishkek, Islamabad, Bangkok and Beijing

Mid-Term Review of CAREC 2020 A Discussion Note

I. Introduction

1. **CAREC 2020.** The Strategic Framework for the Central Asia Regional Economic Cooperation Program 2011–2020 -- or CAREC 2020 -- was endorsed by the 10th Ministerial Conference in Baku in 2010 to guide CAREC over the coming decade. The Senior Officials Meeting in September 2015 endorsed the conduct of a Mid-Term Review (MTR) of CAREC 2020, to take stock of the progress made towards the strategic objectives and identify adjustments needed in light of changes in the global and regional landscape. The MTR will also provide strategic inputs to the preparation of the next 10-year strategy, CAREC 2030.

2. CAREC 2020 set two strategic objectives, expanded trade and improved competitiveness. Supporting these twin objectives are seven operational level priorities: (i) transport (investments in infrastructure); (ii) trade facilitation (measures to facilitate the movement of goods and people); (iii) trade policy (promoting trade openness); (iv) energy (securing reliable, secure and stable energy supply); (v) economic corridors development (promoting investment, production and trade linkages); (vi) the CAREC Institute (developing knowledge support); and (vii) second-tier areas (social impacts of trade expansion, agriculture and the environment, among others). The 11th Ministerial Conference endorsed the Wuhan Action Plan in 2011, indicating the programs and projects in these areas.

3. **MTR Objectives and Scope.** The purpose of the MTR is to undertake a strategic review of CAREC 2020 at the program and sector levels. This is a review of the strategy, not an evaluation of the CAREC Program. The MTR focuses on the following questions:

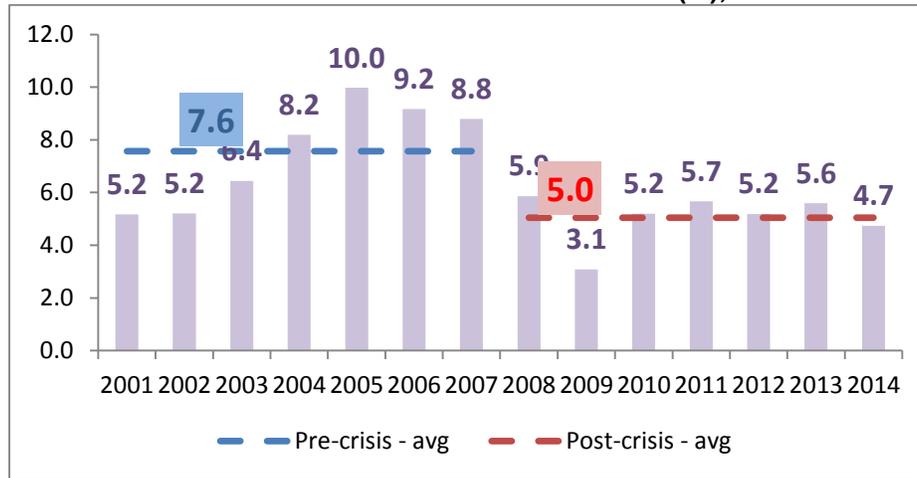
- (i) Has the strategic framework of CAREC 2020 retained its relevance since it was endorsed? Is it, along with associated sector strategies, adequate to achieve the set goals? Are strategic refinements or complementary strategies needed to strengthen the strategic base for the CAREC program beyond CAREC 2020?
- (ii) Are the CAREC 2020 and sector strategies responsive to the development needs of the CAREC countries? Do they remain aligned to national development strategies?
- (iii) What modifications, if any, are needed to the strategy?
- (iv) Has the strategy been followed effectively?
- (v) What has been the implementation performance of CAREC 2020? What are the lessons for improving its implementation?
- (vi) Have the CAREC institutions and mechanisms performed adequately to ensure effective implementation of the strategies? What changes, if any, are needed?
- (vii) Have the stakeholders (national and local governments, private sector, working groups, development partners) played their roles? If not, what needs to be done?

II. Central Asia in the Post-Crisis World

4. The economies of Central Asia grew at an average of 7.6 % from 2001 until the 2008 financial crisis, when growth plummeted. The crisis was immediately felt in the CAREC countries, whose GDP declined sharply between 2007 and 2008. From 2008 to 2013, growth in the CAREC economies averaged 5%, and in 2014 it dipped to 4.7%. The slowdown in export demand, mostly from the Russian Federation, the fall in remittances, and declining revenues for

commodity exporters (Kazakhstan, Mongolia, Tajikistan and Turkmenistan) weighed down the countries' growth performance.

Table 1. GDP Growth of the CAREC Countries* (%), 2001-2014



*Excludes the PRC.

5. Growth has been positive and relatively stable since 2008, but has not recovered to pre-crisis levels. Countries' policy responses have proved inadequate for a more sustainable recovery. Exports remain concentrated on commodities, increasing the vulnerability of exporting countries. The banking system, particularly in Kazakhstan, needs comprehensive reform. The superior infrastructure and labor skills with which countries started the economic transition are no longer adequate. At present, policy obstacles as well as infrastructure, capacity and skill shortages constraint Central Asian economies from achieving strong and sustainable growth.

6. The short-term outlook for the region is not encouraging. ADB estimates that growth in 2016 will slacken in Kazakhstan, Turkmenistan, and Uzbekistan. Fiscal surpluses in the region's oil exporters are expected to weaken. Some countries may contain deficits through spending cuts and improved tax collection, while Azerbaijan, Kazakhstan and Uzbekistan are dipping into reserves built up in recent years to blunt the impact of low oil prices.

7. Fiscal constraints will confront countries with tough choices between cuts in expenditure for education, health and social services, and cuts in investment in infrastructure. The recent devaluation and depreciation of Central Asian currencies have raised the cost of servicing external loans. This could lead to a general reduction in external borrowing. It could also affect debt sustainability and access to international credit, and push the Central Asian countries to rely more on the private sector and public-private partnerships.

8. The CAREC countries have taken modest measures towards structural transformation, including urbanization and economic diversification. However, much remains to be done. The following key characteristics set the CAREC countries apart and highlight areas in most urgent need of action.

- Economic diversification from agriculture to services has been modest. Expansion of services has been limited mainly to mining and retail, which offer limited potential for employment productivity increases. Manufacturing in Central Asia is not competitive

and has failed to diversify. As a result, oil-rich countries have a high degree of product concentration, and resource-poor economies, while more diversified, depend on non-tradables and relatively unsophisticated services.

- Living standards have improved significantly following the surge in the price of oil and other commodities in the 2000s. However, productivity and efficiency remain low and employment growth has declined, hampering competitiveness. The Central Asian economies suffer from significant shortages of skilled labor.
- Compared with other resource-rich economies, Eurasian countries have increased their dependence on natural resources as a source of revenue. Moreover, it was only recently that net savings from these revenues were efficiently invested in physical infrastructure. Previously, a significant portion went to energy subsidies and investments abroad. Despite recent efforts, the quality of infrastructure in Eurasia lags behind many other emerging countries, indicating a significant need for further investment.
- Central Asian economies trade less among themselves than with Europe, which accounts for half of exports and a third of imports. Trade with East Asia is also significant, accounting for a fifth of exports and almost a quarter of imports. The emergence of trade from western China and the possibility of increased trade with the Eurasian Customs Union are opening up new opportunities. However, realizing these benefits, and integrating Central Asia into the global economy, will require better infrastructure, more integrated supply chains, and higher skill levels.

III. Regional and Global Developments Affecting Central Asia

A. Large-scale Resource Mobilization for Infrastructure

9. The Asia-Pacific region is currently witnessing a large-scale mobilization of resources for infrastructure, reflecting changes in the global financial architecture and a concern to address the region's massive infrastructure needs. **The ADB** will expand its annual lending capacity to \$20 billion by 2017.

10. In 2014-2015, emerging economies launched two new multilateral banks, **the Asian Infrastructure Investment Bank (AIIB)** and **the New Development Bank (NDB)**. The AIIB, a PRC initiative, has subscribed capital of \$100 billion to finance infrastructure in Asia. In addition to the PRC and numerous developed countries, the AIIB's founding members include seven other CAREC countries, Azerbaijan, Kazakhstan, the Kyrgyz Republic, Mongolia, Pakistan, Tajikistan, and Uzbekistan. The NDB, led by the five BRICS countries (Brazil, Russia, India, the PRC and South Africa), has subscribed capital of \$50 billion, but is expected to start operations more slowly than the AIIB.

11. The PRC has also launched **the Silk Road Fund** to support its One Belt One Road (OBOR) initiative (para 15). The PRC will contribute \$40 billion to the Fund, which is open to investors.

12. In 2015, Japan announced financing of \$100 billion for "quality infrastructure", to be coursed through the **Japan International Cooperation Agency** and **the Japan Bank for International Cooperation**. In addition, Japan and ADB have a partnership to provide \$16 billion in resources to support infrastructure throughout Asia, leveraged with investments through public-private partnership arrangements.

13. Resources mobilized through these initiatives will significantly increase financing for infrastructure, and will be supplemented by initiatives by the Republic of Korea and the US. However, the figures pale in comparison with the estimated \$800 billion in investment required annually for infrastructure in Asia. Moreover, the current volatile economic environment may limit the extent to which commitments are translated into funding.

B. New Mega-Frameworks for Regional Cooperation and Integration

14. The commitment of new resources goes hand in hand with the launching of several comprehensive frameworks for regional cooperation. Due to its strategic location between Europe and Asia, and its significant oil and gas deposits, Central Asia is the focus of several of these initiatives.

15. The OBOR was proposed during PRC leaders' visits to Central and Southeast Asian countries in 2013. The OBOR is a massive intercontinental initiative that maps out the links between the PRC and the rest of the world. It has two pillars, the "belt", which is a complex of railways, highways, and oil and gas pipelines that would run from western PRC through Central Asia (traversing Kazakhstan and Mongolia), linking to Russia and Europe. The "road" consists of a network of ports and other coastal infrastructure from PRC's eastern seaboard stretching to Southeast Asia, South Asia, and the Gulf, terminating in Europe and East Africa. Central Asia is critical in the OBOR initiative because of its strategic location.

16. The US has also launched the "New Silk Road for Central Asia and Afghanistan", to integrate the region and promote it as a link between Europe and East Asia. The initiative focuses on energy markets, trade and transport, customs and border operations, and business development. With transition underway in Afghanistan, the US and its allies hope to bolster peace and stability by supporting trade and opening new markets connecting Afghanistan to Central and South Asia, and beyond.

17. In 2013, Korea announced its Eurasia Initiative as an infrastructure and energy link between Asia and Europe. Korea proposes rail and road networks through Asia to Europe, and new sea routes through the Arctic Ocean. Transport integration will be followed by trade integration, leading to the establishment of a vast free trade zone.

18. The PRC and Russian have also firmed up their cooperation in the region. At the BRICS and Shanghai Cooperation Organization (SCO) summit held in the Russian city of Ufa in July 2015, they agreed to expand the role of the SCO linking OBOR and the Eurasian Economic Union (EAEU). The PRC called for more collaboration between the SCO, BRICS and the EAEU, with Central Asia and Mongolia as bridgeheads. The SCO is also expanding to South Asia, with India and Pakistan expected to join in 2016.

C. The Changing Regional Cooperation landscape in Central Asia

19. The CAREC Program is one of the largest, if not the largest, regional cooperation initiatives in Central Asia. It has a solid track record of accomplishments, and a well-developed institutional framework. The institutional mechanisms for the mega frameworks have yet to take shape. However, it is clear that the rapidly changing regional cooperation landscape will raise

questions of coordination and may challenge exiting institutional mechanisms. This is an issue for which CAREC should be prepared.

IV. The CAREC Program: A Quick Look Back

20. **A Snapshot of Accomplishments.** Over the past 15 years, the CAREC Program has grown from six transport projects worth \$247 million in 2001, to 166 projects with a total cost of \$28 billion in 2015. Much has been accomplished in the four priority areas of cooperation. In transport, more than 11,000 km of roads have been built; 1,036 km of new railways were constructed, and 317 km of railways improved. In trade facilitation, road border crossing time has been reduced from an average of 8.9 to 5.6 hours; border clearing time, from 10.9 to 10.0 hours; and measures to simplify, automate and modernize customs are making progress.

21. In energy, investments in power generation and interconnection are addressing uneven distribution and variations in power supply and promoting cross-border trade in electricity. In trade policy, barriers to trade in goods and services are being dismantled by promoting accession to the World Trade Organization. A pilot initiative in economic corridor development is underway between the cities of Almaty and Bishkek. The physical base of the CAREC Institute has been established in Urumqi, and operations started in July 2015.

V. The Way Forward: Key Questions

22. Looking ahead to 2017–2020 and beyond, we would like to seek your guidance on four key questions. We also welcome your inputs on issues not covered by the questions below.

23. **Question 1: Transport and infrastructure initiatives.** CAREC has a successful track record of supporting roads and railways, and trade facilitation. With numerous large-scale new initiatives in infrastructure development (OBOR, AIB, Japan, Korea, etc.), how should CAREC position itself? What steps should CAREC take? The Almaty-Bishkek corridor provides a model for leveraging connectivity with highly productive economic activities. Does such a model have wider applicability in the region? Can CAREC move from infrastructure corridors to economic corridors providing a wider range of support?

24. **Question 2: Broadening the CAREC Agenda.** The current volatile global and regional economic environment highlights the importance of economic diversification. Transport infrastructure, connectivity and trade facilitation may not be the only priorities. Lessons learned by the ADB from the Greater Mekong Subregion highlight the importance of going beyond transport corridors and trade. Do the twin objectives on increased trade and enhanced competitiveness remain relevant? How can the CAREC agenda be broadened to address current and future needs? How can CAREC support economic diversification? Should CAREC support education, skill development, job creation and strengthening regional labor markets? Are there other areas in which CAREC could play a role?

25. **Question 3: Institutional Challenges (External).** The new financial and infrastructure initiatives bring new players into regional cooperation in Central Asia. How should CAREC respond to the new initiatives? Should it collaborate, compete, or adapt its product portfolio (to be complementary)? Should CAREC position itself as coordinator for the new initiatives? What changes in the CAREC institutional framework are needed to adapt to these new developments?

26. **Institutional challenges (Internal).** CAREC also faces internal institutional challenges. How can CAREC enhance the effectiveness of its institutions? How can the role of the working groups, SOM and Ministerial Conference be improved? What next steps should be taken with the CAREC Institute? And how can the role of the CAREC Secretariat be strengthened?

27. **Question 4: Beyond CAREC 2020?** The current strategy, CAREC 2020, covers the period 2011–2020. The MTR will make recommendations for the remainder of the strategy period (2017–2020). Now is also the time to think ahead, beyond the current strategy and lay the groundwork for CAREC 2030. Looking ahead, what strategic work should CAREC carry out in 2017–2020 to pave the way for the future beyond 2020?

VI. Next Steps

28. The MTR of CAREC 2020 will involve a consultative process with CAREC governments, academics, think tanks and the sector coordinating committees. The MTR will be presented for the review of the Senior Officials' Meeting in July 2016, and to the 15th Ministerial Meeting in the 4th quarter of 2016 for consideration and endorsement. Below is the indicative timeline.

Activity	Milestone Date
1. Brainstorming Workshop	December 2015
2. Review/inputs by Sector Coordinating Committees	1st Quarter 2016
3. Institutional Review by CAREC Secretariat	1st Quarter 2016
4. Country and Sector Consultations	April–June 2016
5. CAREC Senior Officials' Meeting	July 2016
6. Special NFP Meeting	September 2016
7. 15th CAREC Ministerial Meeting	4th Quarter 2016