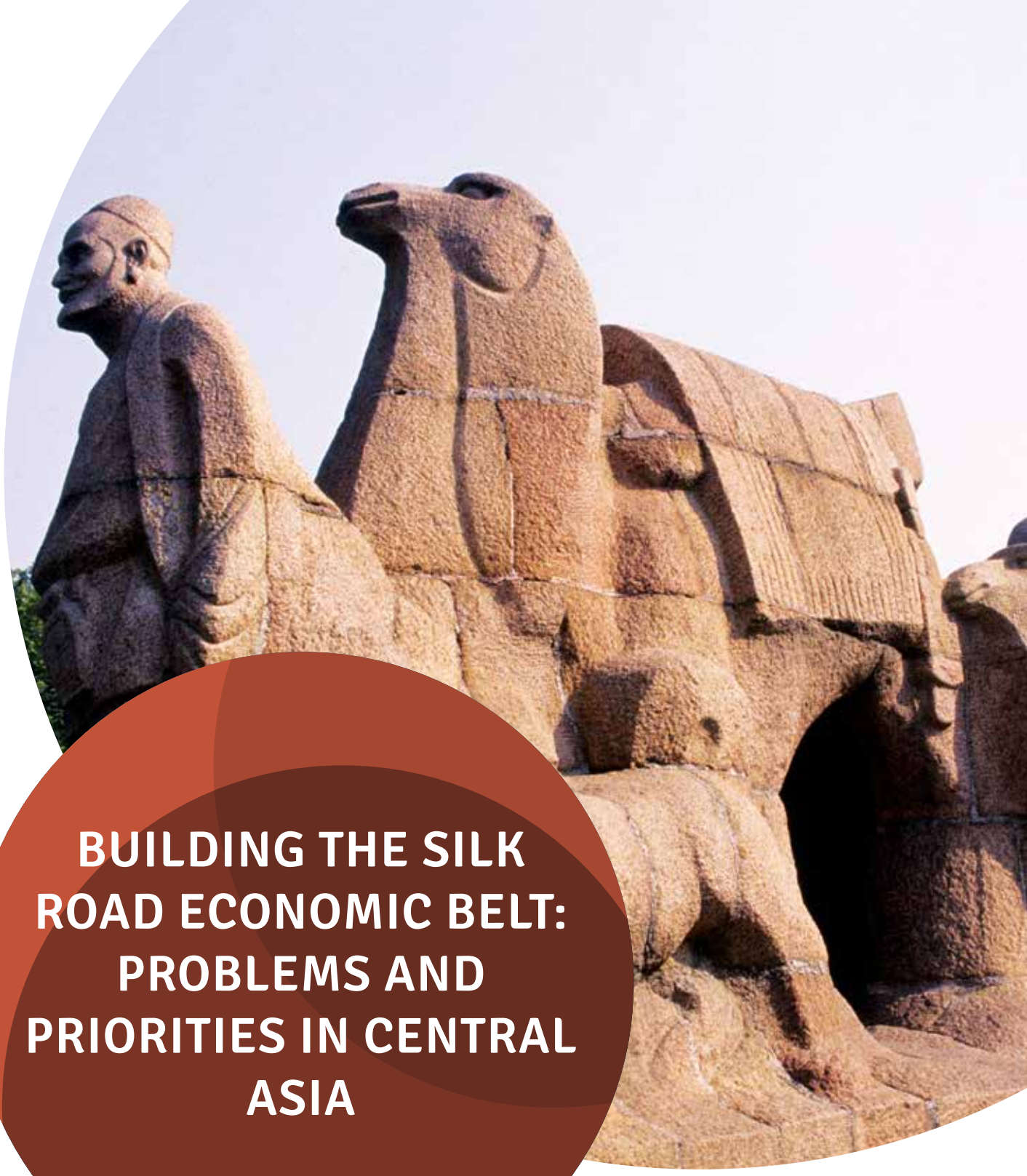

BUILDING THE SILK ROAD ECONOMIC BELT: PROBLEMS AND PRIORITIES IN CENTRAL ASIA

Policy Report

May 2015

Zhang Hongzhou

RSiS Nanyang Technological University | S. RAJARATNAM SCHOOL OF INTERNATIONAL STUDIES

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Executive Summary

Central Asia occupies the centrepiece of China's Silk Road Economic Belt (SREB) initiative. Yet, reviving the Silk Road in Central Asia will not be easy and the geopolitical challenges will be the biggest hurdle to building the SREB in the region. The idea of Central Asia as a regional grouping in political and security terms is almost non-existent and Central Asian countries remain widely divided with serious internal conflicts caused by unresolved boundary, water and energy disputes, regional rivalry, deep mistrust and differences in political, diplomatic and security policies. Also, there is an on-going big power game in Central Asia. In recent years, while better trade and investment ties with all five Central Asian countries boosted China's economic influence in Central Asia, China is still far from being a dominant force in Central Asian affairs because of the influence of Russia and, to a lesser extent, the United States. In the near to medium term, China still cannot compete with Russia which had a significant head start in the region.

In terms of responses to China's SREB, Central Asian countries are excited about economic opportunities that China's SREB brings, but at the same time, wary of the geopolitical implications of China's expanding economic influence in the region. Similarly, Russia has mixed feelings towards China's SREB. Given Moscow-centred economic and political integration projects such as EEU and CSTO, Moscow is not likely to support the SREB project in Central Asia. In contrast, as U.S. influence wanes in Central Asia, the United States is less concerned even though the SREB is in direct competition with its New Silk Road Project and seems to be adopting an open attitude towards the SREB. Against this economic and geopolitical backdrop in Central Asia, this paper suggests that China needs to pay attention to the following aspects in building the SREB.

First, building the SREB should be a gradual and incremental process. Deeply rooted internal conflicts in Central Asia as well as the presence of big powers in the region can block China's efforts to build the SREB. Social instability, poverty, corruption, leadership transition, and social conflicts pose high risks and uncertainty to the Chinese investment. Thus, both China's central and local governments need to understand that being eager for quick success might lead to political backlash and a careful and incremental approach is needed. It is better to build momentum with smaller projects first and seek the opportunity to connect the "dots" at a later phase.

Second, a bilateral approach is preferred. Instead of focusing on grand-scale projects involving many countries, China should adopt a bilateral approach by engaging in economic, social, cultural and even political and security cooperation with individual Central Asian countries. In this way, policies can be customised for individual countries, taking into account country-specific interests and limitations.

Third, agricultural cooperation offers huge potential. Unlike energy investment which largely benefits the Central Asian elites, agricultural cooperation has the potential of bringing wider economic benefits to ordinary people. Given the food insecurity in Central Asia, Chinese financial investment, agricultural R&D and technology will ensure regional food supply and enhance regional stability. In addition, agricultural modernisation will help keep regional water conflicts under control.

Fourth, to finance projects under the framework of the "One Belt, One Road" initiative, China introduced two key financial instruments—the Asian Infrastructure Investment Bank (AIIB) and the 40 billion dollar Silk Road Fund. As far as funding projects in Central Asia is concerned, the Silk Road Fund is the better financial instrument.

Fifth, in the long run, China needs to integrate Central Asia into the Pan Asia Production Network. To overcome challenges to the Sino-Central Asian economic cooperation, economic restructuring of Central Asian countries and China's western provinces is needed to build a regional supply chain to minimise direct competition.

Introduction

The Silk Road Economic Belt (SREB) proposed by Chinese president Xi Jinping during his visits to Central Asia in September 2013 is considered as one of his two most significant diplomatic initiatives.[1] The SREB aims at expanding China's economic connections—perhaps political influence too—across much of Eurasia through vast infrastructure and investment schemes.

The SREB potentially involves over 40 Asian and European countries with the centrepiece of the Belt occupied by Central Asia. As the former hub of the ancient Silk Road, Central Asia will once again play a major role in the success of constructing the SREB. While the SREB is essentially about enhancing economic cooperation and building closer and deeper economic ties between China and countries in Central Asia, reviving the Silk Road in Central Asia will not be easy and the geopolitical challenges will be the biggest hurdle to building the SREB in the region. As China is making all-round efforts to push forward its SREB initiatives, a better understanding of the complex relations among Central Asian countries as well as big power politics in the region will be critical to the future success of the SREB.

This paper, thus, intends to provide a preliminary assessment of the internal dynamics and external interests in Central Asia and its implications for China's SREB. Towards this purpose, the rest of the paper is organised as follows. The second section covers an analysis of internal power dynamics in Central Asia. The third section comprises a discussion of big power politics in Central Asia. In the fourth section, each party's response towards the SREB is discussed. In the last section, policy recommendations on approaches and priorities of constructing the SREB are presented.

1 The other one is the Maritime Silk Road of the 21st Century.

Central Asia is deeply divided

"Central Asia", a term which frequently appears in international newspapers, scholarly articles and speeches by political leaders around the globe, encompasses five former Soviet republics: Kazakhstan, Kyrgyzstan, Tajikistan, Turkmenistan and Uzbekistan. Even if these five countries share many similarities in terms of geographic location, culture, language, history and religion, it is wrong to view Central Asia as a single regional grouping with similar economic, political and foreign policies. After the fall of the Soviet Union, the two largest Central Asian states of Kazakhstan and Uzbekistan attempted to push for greater regional cooperation and integration. In January 1994, an agreement was signed in Tashkent for the creation of a Central Asian Union, with Kyrgyzstan joining shortly thereafter. This marked the start of Central Asia's economic integration through development and implementation of economic projects. After two decades, due to internal differences among Central Asian states and the influence of external powers, Central Asian integration became a dead concept.[2]

What's worse is that cooperation among the five Central Asian countries is hindered by challenges posed by the following: (i) craze for national sovereignty and differences in foreign political agendas; (ii) escalation of border and water disputes and; (iii) internal rivalry.

First, owing to their very short history of independence, all the leaders of Central Asian nations prize their country's sovereignty. Building national solidarity and autonomy in foreign policy making is, understandably, the top priority. For instance, in Kazakhstan, "national security" and "domestic political stability and the consolidation of society" were listed as the top two priorities in the "Kazakhstan 2030" strategy for development.[3] The subsequent "Kazakhstan 2050 Strategy" is aimed at joining the club of the 30 most developed countries of the world by 2050 by means of "strengthening the statehood" and "new Kazakhstan patriotism". Similarly, Uzbekistan has been pursuing a policy of nation-building to define the new state internally as well as externally. Both examples suggest that policy makers in Central Asia crave for sovereignty and retain their differences in political agendas.

Second, the incomplete delineation of boundaries following the collapse of the Soviet Union left all five countries with border disputes of varying degrees with each other. The most contentious area is in the Ferghana Valley where Tajikistan, Uzbekistan and Kyrgyzstan make historical claims to pieces of land in one another's territories, resulting in a series of inter-state conflicts.[4] From 2012 to 2013, 38 security incidents occurred on the Kyrgyz-Uzbek border while 37 occurred on the Kyrgyz-Tajik border.[5] Recent records suggest that the rate of incidents among largely non-demarcated borders in the area doubled in 2014.[6] In the Ferghana Valley, some of the border disputes which included clashes among local communities of the respective countries easily escalated into clashes involving armed skirmishes between border troops, resulting in prolonged border closures and tense security conditions. Such conditions weakened the already poor inter-state collaboration as well as hampered intra- and inter-regional trade in Central Asia.

Besides border disputes, water dispute is also a major source of tension. Water has always been the most precious resource in Central Asia. Both Syr Darya and Amu Darya rivers account for 90 per cent of Central Asia's river water and supply 75 per cent of the water needed for its irrigated agriculture. Although Kyrgyzstan and Tajikistan occupy just 20 per cent of the Aral Sea basin, 80 per cent of the regional water resources flow from this territory. The Kyrgyz people control the downstream flow of Syr Darya at the Toktogul dam and reservoir. Tajikistan intermittently built the Rogun dam on Vakhsh, a major Amu Drya tributary.[7] The lack of a viable regional system to

2 Nurzhan Zhambekov. "Central Asian Union and the Obstacles to Integration in Central Asia" *Analytical Articles.* 2015.

3 See the "The Strategy for development of the Republic of Kazakhstan" available at http://www.akorda.kz/en/category/gos_programmi_razvitiya

4 International Crisis Group. "Water Pressures in Central Asia". *Europe and Central Asia Report N°233.* 2014

5 Ibid

6 Casey Michel. "Drop in Migrants Remittances a Problem for Central Asian Economies" *The Diplomat*. 23 December, 2014

7 International Crisis Group. "Water Pressures in Central Asia". *Europe and Central Asia Report N°233.* 2014

replace the Soviet system of water management led to armed conflict and clashes over competition for water resources between Kyrgyzstan, Tajikistan and Uzbekistan. Islam Karimov, the President of Uzbekistan, openly warned that fulfilling dam building plans without regard for downstream countries like Uzbekistan and Kazakhstan could lead to wars.[8] Although a full-blown water war seems unlikely, any water dispute will undoubtedly challenge cooperation among the three countries.

Third, unlike Southeast Asia where Indonesia is the recognised leader with some relatively keen, albeit declining, interest for regional integration,[9] in Central Asia, Kazakhstan and Uzbekistan are vying for regional leadership. The former is the economic powerhouse with the largest territory in Central Asia; the latter is the most populous country with a strong army. At an official level, it seems that bilateral relations improved in recent years. In June 2013, when Kazakh president Nursultan Nazarbayev visited Tashkent, both countries established a strategic partnership. Similarly, in November 2014, when Uzbek president Islam Karimov visited Kazakhstan, the two countries agreed to strengthen their strategic partnership and enhance bilateral cooperation in trade, economics, cultural, humanitarian and other areas.

However, the truth is that these two countries have very different strategic and foreign policy preferences and cannot get along well with each other. As pointed out by Farkhod Tolipov, relationship between the two countries has long been soured by their tussle for regional primacy in Central Asia. In terms of foreign policy strategy, Kazakhstan pursues a multi-vector policy favouring closer economic, political and security ties with external players, particularly Russia, whereas Uzbekistan prefers bilateralism and independent political and security policies. Their differences in foreign policy approaches led to their diminished roles in regional affairs and greatly limited their capacity for regional leadership.[10]

Both countries also have very different economic, political and security policy priorities. For instance, in the security arena, after the U.S. withdrawal, Kazakhstan's position on post-2014 Afghanistan is relatively calm whereas Uzbekistan is extremely concerned about the possibility of a spillover of extremist and terrorist activity from Afghanistan's territory into Central Asia.[11] Besides, Kazakhstan has close ties with Russia and is supportive of Russia-led economic and security cooperation in the region. In contrast, Uzbekistan has been trying to distance itself from Russia.

8 Refer to "Uzbek leader sounds warning over Central Asia water disputes", available at http://www.reuters.com/article/2012/09/07/centralasia-water-idUSL6E8K793I20120907

9 For many decades, Indonesia had put ASEAN as the cornerstone of its foreign policy and outlook, but under the current Jokovi administration which appears to be taking more bilateral, domestic-oriented foreign policy relative to his predecessors with a diminished but still important role for ASEAN; Dewi F. Anwar. "Indonesia's Cautious Confidence" *Project Syndicate*. 16 July 2013, and Prashanth Parameswaran. " Is Indonesia Turning Away From ASEAN Under Jokowi?". *The Diplomat*. 28 December 2014

10 Farkhod Tolipov. "Uzbekistan and Kazakhstan: Competitors, Strategic Partners, Eternal friends" *Analytical Articles* 2013.

11 Ibid; Roger N. McDermott. "Central Asian Security Post-2014: perspectives in Kazakhstan and Uzbekistan", *DIIS Report* 2013

External power presence in Central Asia[12]

In recent years, after investing billions of dollars across the region, as China becomes the number one trading partner of most of the Central Asian countries, some commentators claim that China is now the dominant power in Central Asia.[13] Despite the recent phenomenal growth in trade and investment, China's rising influence in the region is still far from making Central Asia its own "backyard". The influence of Russia and, to a lesser extent, the United States on regional affairs should not be overlooked.

Russia continues to dominate

Despite China's growing economic influence in Central Asia, Russia will continue to play a substantial role in the region through a combination of energy, culture and military bonds that run too deep for China to severe in the short to medium term.[14] China lags behind Russia in commanding Central Asia's direction in moving forward.

Economically, while China has emerged as the region's number one trading partner and investor, Russia remains a dominant economic force in Central Asia. Due to the very close energy ties with Central Asian countries, China managed to secure enough Central Asian gas to meet 40 per cent of the country's total gas imports by expanding the Sino-Central Asian gas pipeline. Since 2009 when the pipeline came online, Central Asian gas exports to Russia dropped by nearly 60 per cent.[15] However, Russia continues to play a bigger role than China in the Central Asian oil market. Kazakhstan's two largest oil pipelines (with a combined export capacity of 1.42 million bpd) terminate on Russian territory, in Novorossiysk and in Samara. The Kazakh-China pipeline will be expanded to an export capacity of 400,000 barrels per day.

In addition, Tajikistan imports 90 per cent of all petroleum products from the Russian Federation, while neighbouring Kyrgyzstan brings in 92 per cent of its fuel from Russia. Uzbekistan, with the region's largest population of 28 million people, consumes mostly internally produced natural gas but exports more than half of its remaining gas through Russia.[16]

Russia's economic dominance in Central Asia is more prominent given the reliance of Central Asian countries on migrant remittance from Russia. About 1 million Kyrgyz citizens and over 1 million Tajiks (about half of each country's workforce) work in Russia. Tajikistan, a country with 8 million people, has been able to regain stability after the 1992–97 civil war because many of its citizens are earning a living in Russia. The same goes for Kyrgyzstan, a country of less than 6 million and where two presidents have been overthrown since 2005.[17] According to World Bank data, migrant remittance from Russia accounted for 25 per cent of the GDP in 2013 for both Tajikistan and Kyrgyzstan, and 12 per cent for Uzbekistan.[18] While Russia's recent economic crisis and drop in the Ruble value has led to notable reduction of migrant remittance to these Central Asian countries,[19] a significant portion of their GDP will continue to come from remittance from Russia given there is limited employment opportunities domestically and elsewhere, except Russia.

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12 Besides, Russia and the United States, EU, Iran, India and Turkey are also important players in the region as well. For instance, Turkey has been expanding its influence in Central Asia; its soft power over the years has achieved a moderate level of success, especially in Kazakhstan and Kyrgyzstan. Nonetheless, their roles are confined when compared with big powers like Russia and the United States.

13 Casey Michel. "China Edging Russia out of Central Asia". *The Diplomat.* 11 November 2014; see "Central Asia is China's Backyard, Not Russia's" available at http://www.themoscowtimes.com/opinion/article/central-asia-is-chinas-backyard-not-russias/502470.html; see " Putin Is Losing Out to China in Central Asia's Latest 'Great Game" available at http://www.bloomberg.com/bw/articles/2014-11-06/putin-loses-his-grip-on-central-asia-as-china-moves-in.

14 Garret Mitchell. "China in Central Asia: the Beginning of the end for Russia?". SLOVO, 2014. Volume. 26, No. 1

15 Casey Michel. "China Edging Russia out of Central Asia". *The Diplomat.* 11 November 2014

16 Garret Mitchell. "China in Central Asia: the Beginning of the end for Russia?". SLOVO, 2014. Volume. 26, No. 1

17 James Sherr. "How to Suborn Great Powers". *Asia Policy*. 2013. Volume 16

18 See "Russia's rouble crisis poses threat to nine countries relying on remittances" available at http://www.theguardian.com/world/2015/jan/18/russia-rouble-threat-nine-countries-remittances

19 See "Central Asian migrants feel the pain of Russia's economic downturn", available at http://www.reuters.com/article/2014/12/02/us-europe-demographics-centralasia-idUSKCN0JG13S20141202

In addition, Russia's ability to advance a Moscow-centred regional economic integration framework also promotes Russian economic supremacy over Chinese in Central Asia. On the one hand, since 2003, the Chinese concept of SCO (Shanghai Cooperation Organization) free trade zone has not materialised because of the lack of support among member countries.[20] On the other hand, in 2010, Russia successfully established a Moscow-centred Eurasian Customs Union which was upgraded in May 2014 to the Eurasian Economic Union (EEU). The EEU comprises members such as Russia, Belarus, Kazakhstan and Armenia, with Kyrgyzstan set to join from 1 May 2015, and possibly Tajikistan and Turkey. The objective of the EEU, argued by Chris Devonshire-Ellis, is to establish a bloc of ex-Soviet states — the Eastern European and Central Asian version of the European Union — to create a single market for goods and services among members.[21] The EEU could serve as a potential threat to Sino-Central Asian economic ties.[22]

In the political and security arena, Russia's dominance is even clearer. Five Central Asian countries were all founding members of the Russian-centred Commonwealth of Independent States (CIS). Member countries interact within the CIS through its coordinating institutions such as Council of Heads of State, the Council of Heads of Government and the Councils of Foreign Ministers and Defence Ministers to promote regional cooperation on various issues. Under the framework of the CIS, Russia has enhanced its leading military role through the formation of the Collective Security Treaty Organization (CSTO) in Central Asia. In recent years, Russia has expanded defence capabilities, legal mandate, and a range of missions of CSTO in the region. At the forefront of these efforts is a Russia-led plan to create a new CSTO Rapid Reaction Force (RRF) and a larger Central Asian Military Group.[23] As CSTO is evolving into a more coherent organisation, Jeffrey Mankoff argues that political and security integration via CSTO provides Russia an avenue for direct intervention in Central Asia.[24] Withdrawing NATO from Central Asia after 2014 further enhanced the Russia-led CSTO as the dominating security force in the region. In comparison, the China-centred SCO does not provide any security presence in Central Asia.

Lastly, the biggest advantage of Russia in Central Asia is supported, perhaps, by the fact that Central Asia represents one of the last locations in the world where Russia exerts soft power. Russian is the dominant language in Central Asia and many of the Central Asian elites were educated in Russia and have developed close connections with Russian leaders. Even if one does not count the intra-elites and institutional linkages that survived the Soviet dissolution, there are still many ethnic Russians living in Central Asia. While the number of ethnic Russians residing in Central Asia has notably decreased since the collapse of the Soviet Union, their combined total currently stands at about 7 million. The vast majority continues to live in Kazakhstan—about 4 million Russians (representing 21 per cent of the country's total population). Ethnic Russians make up 12 per cent of the population in Kyrgyzstan, 6 per cent in Uzbekistan, 4 per cent in Turkmenistan and 1 per cent in Tajikistan.[25]

In a word, as argued by Garret Mitchell, while substantive Chinese inroads into the Central Asian economy should not be discredited, Russia continues to enjoy a privileged regional position, taking into account the importance of foreign remittances, language, fuel transfers, pipeline networks and security contacts.[26]

The influence of United States is declining, but still matters

After 9/11, Central Asia has been on the frontline of the U.S. global strategy during the decade-long war against terrorism in Afghanistan. U.S. security and political presence in the region was enhanced by

20 Yu Bin. "China-Russia Relations: Putin's Glory and Xi's Dream". *Comparative Connections*. 2014

21 The New Eurasian Economic Union – A China FTA in the Offing? See more at: http://www.china-briefing.com/news/2015/01/09/new-eurasian-economic-union-china-fta-offing.html#sthash.AY2bpMUX.dpuf

22 See more at http://www.chinanews.com/gj/2015/01-02/6930599.shtml

23 John A. Mowchan. "The Militarization of the Collective Security Treaty Organization" *CSL Issue Paper*. 2009. Volume 6–09

24 Jeffrey Mankoff. "The United States and Central Asia in 2014". *CSIS Report*. 2014

25 Garret Mitchell. "China in Central Asia: the Beginning of the end for Russia?". SLOVO, 2014. Volume. 26, No. 1

26 Ibid

improving military and diplomatic ties. However, with the withdrawal of forces from Afghanistan and final closure of the U.S. military base from Kyrgyzstan, both U.S. influence and interest in Central Asia has been in decline. Nonetheless, as far as geopolitics and economic development in Central Asia is concerned, the United States remains an important player and its role should be not overlooked, particularly since Central Asian countries play the balancing game. The closure of its Manas Airbase in Kyrgyzstan in 2014 marks the end of U.S. military presence in Central Asia. Even so, the U.S. still has considerable military presence in the region. Military ties forged by the United States will not disappear overnight and Central Asian countries, though resentful of the U.S. for creating a mess in Afghanistan, still needs U.S. support to deal with the region's rising security challenges. In May 2014, a NATO regional office was opened in the Uzbek capital, Tashkent, aimed to facilitate cooperation between the Alliance and all the countries in the region. One year earlier, in April 2013, the United States agreed to transfer 20 Raven UAVs to boost Uzbekistan's border security capabilities.[27] Similarly, in the case of Kyrgyzstan, the United States left considerable amount of military equipment and facilities after it vacated the Manas base and continues to provide military aid to the country.

To fill the void of a departing military presence, the United States developed the New Silk Road Initiative in 2011 as a means for Afghanistan to integrate further into the region by resuming traditional trading routes and reconstructing significant infrastructure links broken by decades of conflict.[28] The United States and its western allies hope to bolster peace and stability in the region through supporting trade links and helping open new markets connecting Afghanistan to Central Asia, Pakistan, India and beyond. While the majority of experts are sceptical of the prospects of the U.S.-led New Silk Road Initiative,[29] several projects have already found monetary and strategic backing. For example, the Central Asia-South Asia electricity transmission project (CASA-1000) received US$15 million from the United States to build trans-continental power grid lines. There is also talk of a Turkmenistan-Afghanistan-Pakistan-India (TAPI) gas pipeline which could receive support from both the Asian Development Bank and the World Bank.[30] Besides the New Silk Road Initiative, in February 2015, the United States also launched the USAID Strategy for 2015–2019 to help Central Asian countries by significantly increasing cross-border trade and employment opportunities for the poor.[31]

Finally, in Central Asia, the United States is not regarded as a regional hegemon but as a viable balancing force to Russia and China. The United States can help Central Asia to maintain regional balance by giving them room to manoeuvre. Very likely in the future, the Central Asian countries will develop closer ties with the United States to pre-empt growing Chinese economic and political dominance in the region.

27 Roger N. McDermott. "Central Asian Security Post-2014: perspectives in Kazakhstan and Uzbekistan", *DIIS Report* 2013

28 See more at http://www.state.gov/p/sca/ci/af/newsilkroad/.

29 Richard Weitz. "US New Silk Road Initiative Needs Urgent Renewal", *The Central Asia-Caucasus Analyst*. 24 March 2015. Reid Standish. "The United States' Silk Road to Nowhere", Foreign Policy. 29 September 2015

30 Erica Marat. "Following the New Silk Road". *The Diplomat*. 22 October 2014; See "U.S. Support for the New Silk Road", available at http://www.state.gov/p/sca/ci/af/newsilkroad/

31 See "USAID continues supporting Central Asia", available at http://www.timesca.com/news/14986-usaid-continues-supporting-central-asia

Reactions to China's SREB

Central Asia: RMB is welcome but not the Chinese

At the official level, all Central Asian countries welcome China's SREB proposal. Since President Xi announced the SREB proposal in September 2013, presidents and high ranking government officials of all Central Asian countries have publicly expressed enthusiasm in varied degrees. For instance, Kyrgyzstan is willing to strengthen practical cooperation with China by actively participating in the building of the SREB and deepening law-enforcement and security cooperation so as to safeguard regional peace and stability.[32] During an interview, Tajik president Emomali Rahmon stated that Tajikistan welcomes Xi's SREB proposal because it suits the country's national interests. Similarly, at a meeting with Xi in Dushanbe in December 2014, the president of Turkmenistan, Gurbanguly Berdymukhammedov, expressed that Turkmenistan will actively participate in the building of the SREB to improve domestic transportation infrastructure and promote trans-border transportation between Central Asia and China.

Central Asian countries' positive response to the SREB can be easily understood: SREB offers huge economic opportunities much needed by all Central Asian economies amid Russian economic recession and the gloomy global economic outlook. Besides, all Central Asian countries are land-locked economies and mostly poor developing countries (except Kazakhstan) heavily reliant on extracting natural resources such as oil, gas and iron. Fulfilling SREB's basic aims of enhancing connectivity, improving infrastructure, diversifying economic structure as well as boosting trade is also fulfilling Central Asia's desire for economic development. After Xi's announcement of the SREB Initiative and the establishment of the USD 40 billion Silk Road Fund, the Central Asian countries have become very keen on Chinese plans to link Eurasia and Europe because they can earn extra cash from being a "transit hub". Regional countries make infrastructure development a priority. Astana is paying much attention to "Western China-Western Europe" highway and definitely will do the same for the USD 242 billion dollar Beijing-Moscow high-speed rail link passing through Kazakhstan. Even Turkmenistan, while keeping its neutral state status, strives to be as active as possible by supporting the construction of Turkmenistan-Afghanistan-Tajikistan railroad and by expanding trade with Caspian states via the recently launched Kazakhstan-Turkmenistan-Iran railroad.[33]

While Central Asian leaders welcome China's SREB, they have serious concerns about the potential negative impact of closer economic and political ties with China. Currently, although China is now the largest trading partner of Kazakhstan and Turkmenistan and the second largest trading partner of Uzbekistan and Kyrgyzstan, the trading scope remains very narrow: Central Asian countries mainly export fuel and ores to China and import labour-intensive products like textiles and light industrial products. In addition, China's investment in the region also focuses on mining and construction with limited involvement in other sectors. For Central Asian economies, over-reliance on exports of fuel, ores and other natural resources is both risky and unsustainable.

Likewise, while the flood of relatively inexpensive Chinese goods provided poorer residents in countries like Kyrgyzstan with basic necessities like fruits and vegetables and spawned a lucrative cross-border trade for enterprising, individual merchants in cities like Almaty, the domestic manufacturing base continues to shrink. In addition, some believe that the Chinese objective is to seize oil, gas and land resources from the local people in Central Asia. As all countries have expressed their desire and determination to move away from a resource-based economy to develop their own manufacturing sector, China is expected to invest more in Central Asia's non-resource sectors. However, in the meantime, they are deeply concerned that China's growing economic investment could result in the influx of Chinese workers, inciting local resistance against Chinese development projects.

Apart from economic considerations, there is political concern as well. Chinese leaders clearly stated that the SREB is about enhancing connectivity and mutual economic prosperity and that China will never interfere in the domestic affairs of Central

32 See "President Almazbek Atambayev of Kyrgyzstan Meets with Yang Jiechi", available at http://www.chinaembassy.org.sg/eng/jrzg/t1224858.htm

33 Daniyar Kosnazarov. "Sino-Russian 'Division of Labor': Keeping Central Asia Stable" *Silk Road Reporters.* February 16, 2015

Asian nations and never seek a dominant role in regional affairs nor try to nurture a sphere of influence. But political elites and security experts in much of Central Asia are aware that China's growing economic presence can lead to Chinese dominance or interference in regional affairs.[34] According to Mamuka Tsereteli, the director of research at Central Asia–Caucasus Institute at the Johns Hopkins University, the great economic presence of China in Central Asia is partially attributed to Central Asian leaders' strategic balancing of China vis-à-vis Russia and the United States.[35] If this theory holds, China's growing economic influence in the region could force Central Asian countries to hedge against China by leaning towards the United States or Russia. Moreover, if China's economic presence becomes too heavy-handed or pervasive, increasing public opposition will challenge the local leadership.

Construction of the SREB in Central Asia is greatly hindered by the widespread China phobia and China's threat narrative. First, the China phobia is rooted in the historical memories during the Soviet anti-China propaganda. Second, the cheap and inferior quality Chinese products in Central Asian markets have tarnished China's image because the local people tend to regard China-made products as synonymous with fake and shoddy quality.[36] Third, China has promoted Sino-Central Asian relations at the official and elite level, neglecting the civil society and non-governmental organisations. In Central Asia, China's major trade and investment focus is on resources that benefit the government and elites, rather than in economic welfare for the general public. Fourth, Chinese business companies tend to overlook local culture, religion and corporate social responsibility, perpetuating a negative image of China.[37] These companies fail to connect with their host communities because of a preference to concentrate on developing relationships with power brokers in the capital or at the local level. Fifth, China's racial and religion policy towards Uighurs in Xinjiang takes a heavy-handed approach and has caused public resentment among the Central Asian people against China. Sixth, opposition parties in Central Asian countries tend to accuse their governments of either corruption or betrayal of national interests, and as a result, the incumbent administrations' cooperation with China suffers the same fate. Seventh, anti-China reports propagated by Western media and local mainstream media's disregard for China's huge achievements have also undermined China's image in Central Asia.

Russia: a potential spoiler in Central Asia?

On the sidelines of the national legislative annual session on 7th March, China's foreign minister Wang Yi announced that China and Russia will sign an agreement to work on the SREB. He added that "the practical cooperation between China and Russia is based on mutual need and has enormous internal impetus and room for expansion".[38] Many commentators quickly labelled Russia as the core partner in building the SREB. However, a careful analysis of Russia's potential role in the building of the SREB in Central Asia suggests that this optimism is premature.

Undoubtedly, the Sino-Russian relationship has significantly improved in the last couple of years because of several high profile corporation agreements and frequent top leader visits. However, the notable improvement in the relationship is not because of enhanced mutual cost or common strategic aspirations, but rather Russia's increasing alienation from the West and also because of China's mounting energy security concern. As rightly pointed out by Paul Coyer, the current Sino-Russian relationship should be characterised as "intimacy on the surface but mistrust underneath".[39] The deep rooted mistrust between the two countries prevents the formation of a strong and fruitful Sino-Russian partnership.

There is no denial that Russia has expressed interest and support for the SREB. Yet, what needs to be noted is that Russia's interest in the SREB has its geographical limitations. While such cooperation can help develop the Russian Far East, it is concerned that China's influence in Central Asia will expand with the building of the SREB. The Russians welcome the opportunities but remain cautious about the risks of the long-term grand project.

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34 Sarah Lain. "China's strategic presence in Central Asia". *IHS Jane's* 2014

35 Mamuka Tsereteli. "Winners and Losers of Strategic Games in Central Asia". *Asia Policy*. 2014 Volume 16

36 Pan Zhiping. "Silk Road Economic Belt: A Dynamic New Concept for Geopolitics in Central Asia. *CIIS*. 2014

37 Sarah Lain. "China's strategic presence in Central Asia". *IHS Jane's* 2014

38 See more at http://www.china.org.cn/china/NPC_CPPCC_2015/2015-03/08/content_34989730.htm

39 See "Inside the Sino-Russian Alignment: Intimacy on the Surface, Mistrust Underneath", available at http://www.forbes.com/sites/paulcoyer/2014/11/11/the-growing-sino-russian-alignment-intimacy-on-the-surface-mistrust-underneath/

On the one hand, a common transport system (as well as elimination of barriers to trade and investment) between China and Russia looks promising and economically beneficial for Moscow; in 2014, Russian high-rank officials referred to the development plan of transport infrastructure in Russia in the coming decades. In particular, Moscow has already granted 560 billion rubles until 2018 to modernise and increase traffic capacity of the two most important railway arteries of the Russian Far East — Baikal-Amur (BA) and Trans-Siberian (TS) Mainlines. Renovation will be focused at border-crossing points with China and in the direction to ports. BA and TS integration into the project of the SREB will lead to additional Russian transit revenue and further develop the depressed economies of the Far East territories.

Moreover, leaning towards China is vital to help Moscow overcome sanctions and hard economic conditions. It is no coincidence Russia expands its geography of cooperation by conducting negotiations with not only China but also ROK and DPRK. Taking into account the Russian Far East which is falling behind its European counterpart, especially in transport infrastructure, its inclusion into the SREB can become an economic trigger for Russia. It will maximise the potential of advanced economic development zones by moving closer to free trade zone with 9 per cent tax burden (instead of 45 per cent as it is in Russia right now). Moscow's desire to be a part of the SREB is proven by various Chinese-Russian initiatives in terms of facilitating goods movement between the two states. Both parties agreed to a joint construction of one of the biggest ports on the Sea of Japan coast with 60 million tons capacity within 18 km from the Chinese-Russian border. This project is in line with the Russian plan to reconstruct 31 ports to develop transport corridors "Primor'e-1" and "Primor'e-2" to improve the logistics of international goods delivery from China, Japan, Australia and Mongolia until 2017.

Besides, Beijing and Moscow have recently agreed to construct a high-speed railway between the two capitals with an estimated cost of USD 242 billion dollars and bring into line the joint use of the port Slavyanka infrastructure for commercial goods that are trans-shipped from the northeastern provinces of the PRC. Finally, Russia is capable of strengthening its position by opening the Northern Sea Route[40] to contend with another Chinese project—the Maritime Silk Road proposal that Xi submitted to ASEAN countries in October 2013.

On the other hand, however, Russia understands that the SREB will inevitably upset the current balance of power not only in Sino-Russian relations but also in Central Asia. The growing Chinese investment is likely to cause Central Asian states to increase their reliance on Beijing. To maintain its influence in post-Soviet countries, Russia's repeated attempts to block Chinese initiatives could be appraised as a challenge to its dominance in Central Asia. For instance, in the past, Russia hampered the establishment of the SCO Development Bank and SCO free trade zone. For years, China has built railway linkages along its western borders through Central Asia and all the way to the Caspian Sea or Europe. Part of this railway strategy is the 268 km long China-Kyrgyzstan-Uzbekistan (CKU) line which was first conceived in 1997. Despite its potential benefits for member countries, it is still not built, primarily due to objections from Russia which already has its own regional railway strategy—the Trans-Siberian Railway. As China's railway standard is 1435 mm whereas Russian standard is 1520 mm, there is direct competition between these two railway projects. Hence, not surprisingly, it was Russia, not the Central Asian countries, that opposed the CKU railway project. Russia's intensive lobbying against this project apparently worked. The China-Kyrgyzstan-Uzbekistan railway project could never be constructed as long as Russia remains a passive observer or even a spoiler.[41]

Therefore, as the construction of the SREB increases Chinese presence in Central Asia, Russia is likely to become aggressive towards China when it starts to lose its diplomatic grip on the region.[42]

The United States: An unexpected partner?

Certainly, U.S. interest in Central Asia is confined—it has no territorial, economic or resource interest in the region. With the drawdown of military forces from Afghanistan, Central Asia will certainly cease to be on the frontlines of U.S. global strategy, particularly as Washington shifts its focus to the Asia Pacific region.

40 From Asia to Europe across the Arctic

41 Yu Bin. "China-Russia Relations: Putin's Glory and Xi's Dream". Comparative Connections. 2014

42 Virginia Marantidou and Ralh A. Cossa " China and Russia's Great Game in Central Asia", *The National Interest.* 1 October 2014

However, to prevent destabilisation in Afghanistan, the United States made an attempt to promote economic development in South and Central Asia by introducing the New Silk Road Economic Initiative in 2011. However, limited funds hampered its success. As a result, many advocate that the United States cooperates with regional powers, particularly China, to promote regional economic development.

Clearly, there are concerns about the negative implications of China's SREB on U.S. interests in Central Asia and beyond. Many see China's SREB as an approach that challenges U.S. hegemony and as an attempt to rewrite the rules of geopolitical and economic architecture.[43] Some like Nadège Rolland even argued that the SREB could further intensify intra-European divergences over their Asia policy, cause deep differences between the United States and its European allies, and sharpen commercial rivalries.[44] Nonetheless, given the fact that Central Asia's security and stability remains America's top interest, according to Jeffrey Mankoff in a paper in 2013, the United States is in no position to take the lead in securing Central Asia after 2014. The United States already needs cooperation from Russia and other powers to fight against common regional threats. With the current U.S.-Russian standoff and expanding Chinese influence in Central Asia, it is logical for the United States to cooperate with China in Central Asia by either including China in its own Silk Road project or supporting China's SREB. Speaking at the Woodrow Wilson Center in Washington, D.C., on 22 January 2015, Nisha Desai Biswal, Assistant Secretary of State for South and Central Asian Affairs said, "While some paint the United States' New Silk Road initiative as being in competition with China's efforts, but in fact the United States welcome China's constructive engagement and see a great deal of potential complementarity in our efforts."[45]

43 B. R. Deepak. "One Belt One Road": China at the Centre of the Global Geopolitics and Geo-economics?", more at: http://www.southasiaanalysis.org/node/1672#sthash.5FMR8yp8.KOBLFj0d.dpuf

44 China's New Silk Road By Nadège Rolland February 12, 2015

45 See " US welcomes China's constructive engagement in Central Asia—Biswal" available at http://www.timesca.com/news/14902-us-welcomes-china-s-constructive-engagement-in-central-asia-biswal

Conclusion and Policy Recommendations

Central Asia occupies the centrepiece of China's Silk Road Economic Belt (SREB) initiative—one of the pillars of China's international strategy under the new leadership. As Chinese policy makers and scholars debate and draft the detailed road markets and sort out priority projects to build the SREB, it becomes critical to understand the internal and external geopolitical factors which determine the regional development trajectory.

Despite previous attempts from both Central Asian countries and external powers to support regional integration, the idea of Central Asia as a regional grouping in political and security terms is almost non-existent. Central Asian countries remain widely divided with serious internal conflicts caused by unresolved boundary, water and energy disputes, regional rivalry, deep mistrust and differences in political, diplomatic and security policies. Furthermore, Central Asia remains highly vulnerable to both external and internal shocks. External factors such as growing Islamic extremism in the Middle East and the NATO withdrawal from Afghanistan pose severe security challenges to Central Asia. Internal factors such as leadership transition in both Kazakhstan and Uzbekistan, in addition to struggling economic development, undermine regional stability. Furthermore, there is an on-going big power game in Central Asia. In recent years, while better trade and investment ties with all five Central Asian countries boosted China's economic influence in Central Asia, China is far from being a dominant force in Central Asian affairs because of the influence of Russia and, to a lesser extent, the United States. In the near to medium term, China still cannot compete with Russia which had a significant head start in the region. In addition, as Alexander Cooley states, great power games are played according to local rules set by Central Asian leaders who employ the balance of power strategy. In this great power game between China, Russia and the United States in Central Asia, the local leaders, who have been able to manipulate and lay off the economic and security interests of great powers to strengthen the sovereignty of their states, are important actors in their own right.[46]

In terms of responses to China's SREB, Central Asian countries are excited about economic opportunities that China's SREB brings, but at the same time, wary of the geopolitical implications of China's expanding economic influence in the region. Likewise, Russia has mixed feelings towards China's SREB. Cornered by the West, Russia is leaning towards China and is keen to cooperate with China under the SREB framework to develop its Fast East region. Given Moscow-centred economic and political integration projects such as EEU and CSTO in the region, Moscow is not likely to support the SREB project in Central Asia. In contrast, as U.S. influence wanes in Central Asia, the United States is less concerned even though the SREB is in direct competition with its New Silk Road Project. The United States seems to be adopting an open attitude towards the SREB. It is concerned about Central Asian regional stability and economic development. The U.S. also understands that its own version of intra-regional cooperation in South and Central Asia is unlikely to materialise.

Having discussed the internal and external geopolitical factors as well as individual actor's response to China's SREB, here are some recommendations on approaches and priorities for China to adopt in building the SREB.

Gradual and incremental process is needed

Deeply rooted internal conflicts in Central Asia as well as the presence of big powers in the region can block China's efforts to build the SREB. Social instability, poverty, corruption, leadership transition, and social conflicts pose high risks and uncertainty to the Chinese investment. Thus, both central and local governments need to understand that being eager for quick success might lead to political backlash and a careful and incremental approach is needed. It is better to build momentum with smaller projects first and seek opportunity to connect the "dots" at a later phase.

Bilateral approach is preferred

Given the unfavourable conditions of deep regional divide, weak mutual trust, different political and security policy preferences, it seems that a multilateral approach to build the SREB will not work. Therefore,

46 Alexander Cooley. *Great Games, Local Rules: The New Great Power Contest in Central Asia*. Oxford University Press. 2012

instead of focusing on grand-scale projects involving many countries, China should adopt a bilateral approach by engaging in economic, social, cultural and even political and security cooperation with individual Central Asian countries. In this way, policies can be customised for individual countries, taking into account country-specific interests and other limitations.

Moving beyond cooperation in energy to cover other areas that bring larger benefits to the local people in the Central Asian region

While energy cooperation will certainly be the focus of China's SREB plan, agricultural ties between China and Central Asian countries should be a priority too. Unlike energy investment which largely benefit the Central Asian elites, agricultural cooperation has the potential of bringing wider economic benefits to ordinary people. Given the food insecurity in Central Asian states such as Tajikistan and Kyrgyzstan, closer Sino-Central Asian agricultural ties via intra-regional trade, Chinese financial investment, agricultural R&D and technology will ensure regional food supply and enhance regional stability. In addition, agricultural modernisation will help keep regional water conflicts under control. Agriculture accounts for over 70 per cent of the fresh water usage in Central Asia, yet 50–80 per cent of water used for agricultural irrigation is wasted due to faulty irrigation systems. China has the resources, given that its Xinjiang province is known for its advanced water-saving irrigation system, to modernise regional water infrastructure and to promote agricultural trade to address regional spatial water scarcity.

Silk Road Fund is the better instrument to finance projects in Central Asia

To finance projects under the framework of the "One Belt, One Road" initiative, China introduced two key financial instruments—the Asian Infrastructure Investment Bank (AIIB) and the USD 40 billion Silk Road Fund. As far as funding projects in Central Asia is concerned, Silk Road Fund would be the better financial instrument for two major reasons. First, although Russia, which had tried to distance itself from the AIIB, eventually submitted its application after the AIIB gained huge momentum with major European powers, it still has considerable doubts and concerns towards it.[47] Russia is wary that the AIIB interferes in Central Asian affairs where historically the main mediator and financial donor was Russia. For instance, Russia is concerned that the AIIB could shadow its common currency vision in Central Asia. In March 2015, Russian president Vladimir Putin said the EEU should adopt a single currency. However, for China, one of the major objectives of creating the AIIB is to promote RMB internationalisation and given China's economic power and global reach, any common currency along the SREB will very likely be the RMB. Therefore, Russia, now as a founding member of the AIIB, might not fully support China's plan to finance projects in Central Asia, though it will be highly interested to utilise the AIIB to fund infrastructure projects in Siberia and the Far East. Second, while many European countries' joining provided more legitimacy and influence to the AIIB, it also means that China will not be able to dominate the leading decisions and there will be high and stringent criteria to not only include economic viability but also social, environmental and human rights impacts, issues for project selection and restrictions on lending. Yet, given that most Central Asian countries have unstable regimes, corrupt political system, weak governance and poor human rights record, it will be difficult for them to borrow from the AIIB to finance their infrastructure projects.

Integrating Central Asia into the Pan Asia Production Network

To a large extent, growing trade and investment ties between China and East Asian countries (including Japan, South Korea and ASEAN nations) can be attributed to the formation of a Pan-Asian production network that complements China's coastal provinces and neighbouring countries.[48] To overcome the challenges to Sino-Central Asian economic cooperation, economic restructuring of Central Asian countries and China's western provinces is needed to build a regional supply chain to minimise direct competition.

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47 See for instance, "Reasons behind Russia's reluctance to join AIIB: Duowei" available at http://www.wantchinatimes.com/news-subclass-cnt.aspx?id=20150327000002&cid=1102

48 A single product assembled and exported from China is likely to embody knowledge-intensive designs originating from Japan, inputs produced from capital or skill intensive production processes in South Korea, Taiwan, Hong-Kong or Singapore (the Asian NICs), and inputs produced from more labour-intensive methods in one or more of the ASEAN 4 countries including Indonesia, Malaysia, Philippines and Thailand. See more from "Productive Integration Of LDCS Into Regional Supply Chains: The Case of South Asia" by John Serieux.

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