

What's at stake in Central Asia from the war in Ukraine?

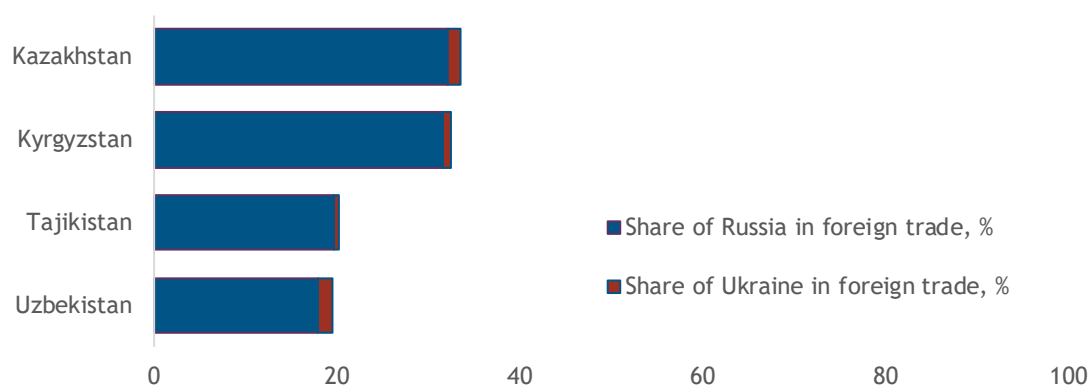
Blog post by Practice Lead for CEE, Russia and Eurasia Alexander Smotrov and Associate Alexander van der Wusten, 7 April 2022

The Russia-Ukraine war was the elephant in the room at the inaugural Tashkent International Investment Forum in late March. While not mentioned directly by the speakers, it was clear to anyone that the conflict will impact Uzbekistan as it tries to position itself as a gateway for foreign corporates and investors to the rest of Central Asia.

The immediate risks for Uzbekistan come from its reliance on Russia, its largest trading partner, for strategic food imports, such as wheat and sugar and from disruptions to sunflower oil supplies from Ukraine. The pressure on the national currency, the so'm, which depreciated in line with the Russian rouble, has cut remittances sent back home by Uzbeks working in Russia. Russia-linked investors - from Uzbek-born tycoon Alisher Usmanov to sanctioned Sovcombank and Gazprombank - seem less welcomed by local authorities and are in some cases perceived as a potentially toxic presence. The transit of goods through Russia has also been disrupted, with Polish apples now not making it to Uzbek markets and stores.

At the same time, the situation opens opportunities for new suppliers and new supply routes. On the forum's sidelines, possible US soybean imports were mentioned, with a potential to establish local soybean oil production as a healthy alternative. A considerable amount of goods trade with Europe could be rerouted via Georgia and Turkey, while India, Pakistan and Afghanistan provide an eastern corridor. However, setting up these new trade routes is a time-consuming process, possibly taking several years, and the products on the shelves could turn out to be more expensive for domestic consumers.

Fig.1. Trade dependence between Russia, Ukraine and Central Asia, 2021



Sources: Eurasian Economic Commission and national trade statistics

Some argue that Uzbekistan's newly acquired GSP+ status as part of the country's WTO accession process could help the country become a trade entrepot and will also be used by Russian companies as a backdoor for exports to European and other markets, which would be very damaging for European relations with Uzbekistan. However, others warn against overestimating the importance of this channel as it is still to be properly developed and used.

For foreign investors, Uzbekistan will try to position itself as an alternative to Russia in certain sectors. For example, with the Russian IT market's attractiveness diminishing, Uzbekistan is already luring Russian and Belarusian IT companies to its market, although it might have difficulty competing with other popular destinations in the region, like Kyrgyzstan.

Uzbekistan's positioning is in part made possible by its neutral geopolitical status, as it is not, unlike its neighbours, part of a Russia-dominated collective security alliance or the Eurasian Economic Union. An unusually unequivocal statement by the Uzbek foreign minister that Tashkent will not recognize the pro-Russian separatist republics in Donbas and calls for a "peaceful solution" to war in Ukraine was strategically timed for the eve of the forum and was noted in Washington and European capitals.

The government is trying to convince investors that it is managing to deal with the impact of the war in Ukraine, that this is just a temporary disruption which will not derail its ambitious reform plans that stretch until at least 2026. While these signals seem to be reassuring, if the government assumes that the economic circumstances will very soon return to the pre-war status and does not work on its mid-to-long-term plan to reorient and reposition the economy away from Russia, the crisis's damage may turn out to be more permanent than previously thought.