

Corruption and Economic Freedom in Central Asian Republics (2001-2008)*

İlyas Sözen, Selahattin Sari, Ahmet Alkan Çelik
Beykent University, Istanbul, Turkey

The aim of this study is to examine the progress of economic freedom and corruption during the period between two global economic crises in those Central Asian Republics which have been integrated into the free market economy according to “the Washington Consensus” since the late 1990s. With respect to the exportation of natural resources, Azerbaijan, Kazakhstan and Turkmenistan together with Kyrgyzstan, Uzbekistan and Tajikistan all seem to have entirely different economic structures. In this paper, the majority of macro-economic variables, economic freedom indicators and corruption data covering the period of 2001-2008 will be discussed. In the light of the outcomes of this study, it is observed that while the social structure in those countries exporting natural resources is stronger, bureaucratic corruption increases consistently in all of the countries due to the authoritarian structures (of the countries concerned). As Central Asian Republics are in a state of failed transition into market economy, the betterment in legislation does not debug the so-called “limbo” system, which refers to neither a planned economy nor a free market one.

Keywords: Washington consensus, Central Asian economy, institutional economics, economics freedom, corruption

Introduction

The stagflation and debt crisis in the 1970s raised some doubts as to the position of government in the market system. Since the beginning of the 1980s, the implementation of neoliberal ideas has led to favorable conditions which direct the socialist and welfare economies towards a competitive market, especially in developed Western economies. In this era, the concept of transition economy, based on socialist thought, should move towards liberalism.

Market economy or liberalism is an economic structure in which market agents can move as they wish; values are determined according to supply and demand, and intervention is not accepted for the balance of formation (Yüce, 2004, p. 1). Since the beginning of the 1980s, neo-liberal policies have been implemented in

* This is a revised version of the paper presented at the International Conference on Eurasian Economics, Beykent University, Istanbul, on November 4-5, 2010.

İlyas Sözen, Ph.D., Assistant Professor, Department of Economics, Beykent University.

Selahattin Sari, Ph.D., Professor, Department of Economics, Beykent University.

Ahmet Alkan Çelik, Ph.D., Assistant Professor, Department of Economics, Beykent University.

Correspondence concerning this article should be addressed to İlyas Sözen, Beykent University, Ayazaga Campus, Sisli, Istanbul, Turkey. E-mail: isozen@beykent.edu.tr.

developed countries especially in the USA and the UK. As a result of the subsequent establishment of the international market through the agency of international organizations in Bretton Woods, developed countries implemented neoliberal policies instead of the developmentalist's conception of the 1970s. The policies implemented were in favour of supply, in an economic conception based on a fundamental argument which says that liberal trade could bring welfare. The neoliberal policy change in the 1980s turned into the Washington Consensus in the 1990s after the problems experienced.

Since the concept of transition economy represents a transformation from a socialist economic system to a market economy system, Central and Eastern European countries, Central Asian countries and Russia which came into being after the dissolution of the Soviet Union are generally accepted as transition economies. In such countries, the policies implemented by the IMF and the World Bank have led to various consequences in terms of the rate of corruption and of economic freedom. In this paper, six Central Asian Turkic Republics were chosen as cases for transition economies where the progress of corruption and economic freedom after the implementation of Washington Consensus in the time of global crisis (2001-2008) will be considered.

The Washington Consensus

In 1989, with the Washington Consensus, J. Williamson put forward the relations of Washington-based institutions (the International Monetary Fund, the World Bank and The Treasury Department of the USA) and advised ten issues of standard reformation for the crisis in developing countries. Williamson noted that the Washington-based institutions were aimed at development of structuring at first, then they accepted the statements of neoliberalists, and these statements turned into market-based policies (Williamson, 2000, p. 251). From then on, the Washington Consensus meant neoliberal policies only.

The International Monetary Fund (IMF) and the World Bank (WB) identified the problems of transition economies after the 1990s as follows (Altay, 2003, p. 11):

- Since there was no democracy, institutional structure was not formed;
- As a result of integrated monopoly, there was cheap, unproductive, and inadequate production;
- With repressed inflation, income distribution was not calculated and there was an imbalance of income distribution;
- Since there was no individual property, trade and demand were insufficient;
- Public expenditures were populist rather than being spent on productive fields;
- Insecurity and corruption were observed with respect to law;
- Social assurances encouraged unemployment and unproductively.

The issues put forward as a response to problems in the Washington Consensus were gathered under the title of stability and liberalization. Although this prescription, accepted by consensus, was initially suggested at the beginnings of the 1990s as a solution to the economic problems of Latin American countries, the same prescription was offered for the transition economies and developing countries in debt crisis at the end of the 1990s with the impact of IMF (Williamson, 2003, p. 324).

The prescription included the following:

- As for macro-economical stability, financial and monetary discipline, priority in public expenditure, tax reform, and competitive exchange rate;

- As for liberalization, price freedom, reduction of government intervention to market system, financial liberalization, privatization, foreign direct investment and property rights.

There were two reasons of the acceptance of the Washington Consensus by transition economies and developing countries. The first reason was the failure of improvement which leaned on import substitution at the end of the 1970s. Another reason was the belief that orthodox policies supported by international organizations like the IMF and the World Bank could solve the failure of economic compensation. The reason for this belief was the dissolution process of the Soviet Union which was the only rival to free market. Washington-based institutions supported the transition economies and also helped the reduction of poverty in developing countries and the increase of the level of wealth by liberalizing capital account (Williamson, 2000, p. 251).

It was observed that the policies implemented under the supervision of the Washington Consensus did not boost growth but caused high inflation. In addition, neither poverty nor economic and social inequality was reduced. After 1998, under the leadership of Stiglitz, it was accepted that the Washington Consensus had failed and the post-Washington Consensus was put forward (Stiglitz, 1998). While the consensus was initially intended for developed countries but subsequently adapted to transition economies, the most important issue was forgotten: the beginning of growth. For the solution of that problem a new understanding was brought forth.

Actually, the post-Washington view seemed to be a continuation of the previous consensus. Based on the ten issues of the previous agreement, ten more issues with social aspects were added in order to correct the deficiencies (Rodrik, 2006, pp. 973-987):

- Institutional governance;
- Anti-corruption;
- Flexibility in labor market;
- World Trade Organizations agreements;
- Financial codes and auditing;
- Cautious expansion of capital accounts;
- Mono (single) exchange rate regime;
- Independent central bank/inflation targeting;
- Surplus of social security;
- Targeting the reduction of poverty.

The ingredients of the new ten issues suggested that the neo-liberal view turned into the institutional view. As a result of the post-Washington Consensus, the importance of institutional structure and corruption for transition economies was realized.

Corruption and Economic Freedom

In 1996, after the annual meeting of the IMF/World Bank, problems of corruption in developing countries indicated that there were many different definitions of corruption. According to the most limited definition by the World Bank (2010), corruption refers to “using civil services for special earnings”. In a report of 2001, since the three-fourths of texts published on corruption of politics and public administration show that (International Transparency Organization, 2001) the qualified definition of World Bank is accepted as a general definition.

There are many definitions of corruption because of the different factors which are effective in corruption

studies. These factors are different cultures, different results of corruption and the wide range of corruption types. Corruption involves different kinds such as bribe, fraud, embezzlement, nepotism, malversation, leaking of commercial information, etc..

In the context of corruption, bribe is the most prevalent one. There are lots of studies on the economic reasons of bribe. Generally, the economic reasons of bribe are (Gürbüz & Dikmenli, 2009, pp. 219-237) the following:

- High inflation (The value of the loss in wage/salary);
- Majority of government in economy (Bureaucratic structure has a higher rate);
- Informal economy (Reduction in the functioning of bureaucracy);
- Inequity in income distribution (Increasing impoverishment);
- Media-trade relationship (Conflict of interests);
- Finance of politics (Rent distribution);
- Lack of transparency in privatization.

In studies focusing on the relationship between rent and public administration, Latin American and African countries are the most representative countries. Rent results in a high rate of corruption; therefore, there are both political and econometric studies on the deterioration of income distribution and politics (Rock & Heidi, 2004, p. 1000).

After the 9/11 events in the US, a security crisis and military conflict occurred all around the world that resulted in the increase in natural resource prices. At the end of 2008, again as a result of the global crisis originating from the US, raw material prices decreased. In the years between 2001-2008, the increase in raw material prices became an additional source for the countries exporting these sources.

In this study, Central Asian Republics were categorized to export of natural resources on which increased natural resource prices after 2001. Azerbaijan, Kazakhstan, Turkmenistan are taken as the first group due to exporting oil and gas, while Kyrgyzstan, Uzbekistan and Tajikistan are taken as the second group since they do not export natural resources.

In the period of 2001-2008, in comparison to the period of 1997-2001, economic growth rate rose almost two-fold in the countries of the first group, but for the countries of the second group there is no difference between the period 2001-2008 and the period 1997-2001 (World Bank). Countries in the first group succeeded in improving their situation thanks to the export of natural resources after the 1997 Asian crisis whereas the countries in the second group maintained their growth at the same rate even though there was overall growth in world trade and economy, suggesting the obvious impact of the natural resources in their economies.

Despite the difficulty in reaching data in Turkmenistan because of the bureaucratic system, an accelerated development and personal income was observed in Turkmenistan when compared to the other countries in the region. Uzbekistan, which has the highest foreign investment stock, is another attractive country despite its high population, weak economy and low personal income. Being an agricultural country, Uzbekistan's trade is based on cotton, hence the level of personal income.

It could be argued that, among Central Asian Republics, Kazakhstan is the most successful country in privatization which results from natural resource abundance and good governance. In the same way, oil and natural gas of Azerbaijan and gold resources of Uzbekistan are effective in privatization and the attraction of

foreign investment to these countries.

The main resource of economic growth is savings. However, these countries need foreign investment not only because of their low socio-economic level of population, but also because of reduced income. In addition to these, since a great portion of foreign investment coming to these countries directs resources like oil, gas, etc., rising money supply increases inflation. Rising inflation affects the income distribution of these countries. In those countries with weak economies and high inflation, the imbalance between the rich and the poor becomes even more obvious, as seen in Table 1 where only thirty percent of the populations take a share from the national economy.

Table 1

Major Macroeconomic Variables

	Azerbaijan	Kazakhstan	Turkmenistan	Kyrgyzstan	Uzbekistan	Tajikistan
Growth (2001-2008) (%)	16.4	9.3	14.3	4.75	6.6	8.7
GDP per capita (2008) (Atlas US \$)	1,605	3,111	1,867	457	584	325
Inflation percent (2001-2008) (%)	8.6	9	15.7	9.2	15.3	7.6
30% Upper income (2008)	48	64	n/a	69	71	66
Privatization (2001-2008) (US \$ million)	191	2,738	n/a	2	70	1
FDI (2008) (GDP) (%)	18.5	45	53.7	20.1	11.2	34.8

Note. Source: Data from the WB, the IMF and the UNCTAD.

The World Bank, Transparency International, the Political Risk Service Group, the World Economic Forum and Global Integrity Organizations have several studies including different types of indicators on corruption. Since 1995, countries are categorized based on the International Transparency Organization (NORAD, 2009, p. 47). This organization determines the indices by asking questions to both business leaders and country analysts. Though the ranking of this organization is not certain, this ranking is widely used to indicate the level of bribe.

As seen in Table 2, while there were totally 91 countries in the bribery index in 2001, by 2008 almost all the countries in the world had been included in this index. Corruption problems of Central Asian Countries are seen clearly both in 2001 and in 2008. The addition of new countries did not make any difference in the index. According to the Corruption Reports of the International Transparency Organization, in the years from 2004 to 2008, while Kazakhstan, Azerbaijan and Tajikistan remained at the same level, Uzbekistan, Kyrgyzstan and Turkmenistan showed a decline of 0.5, 0.4, 0.2 respectively (International Transparency Reports).

Table 2

Corruption Ranking of Countries

	2001	2002	2003	2004	2005	2006	2007	2008
Azerbaijan	84	95	125	140	137	130	150	159
Kazakhstan	73	88	101	124	110	111	155	145
Turkmenistan	n/a	n/a	n/a	139	157	151	166	168
Kyrgyzstan	n/a	n/a	118	125	134	145	157	167
Uzbekistan	74	69	103	114	143	155	176	169
Tajikistan	n/a	n/a	128	138	150	149	160	157
All world	91	102	133	146	159	163	180	182

Note. Source: Statistics are compiled from the International Transparency Reports (2001, 2002, 2003, 2004, 2005, 2006, 2007, 2008).

When their economic structures were taken into account as in Table 1, Tajikistan and Turkmenistan exhibit differences in their situation. Tajikistan is in the same situation with the more developed Central Asian Republics because of its economy and also the rent, which is the main source of bribe, is not shared by all the social groups in the system. In Turkmenistan it is accepted that corruption is a regional problem (CIA, Factbook). Because the export of natural resources and agricultural products in the country is increasing, its economic rent rises gradually as well. According to the International Transparency Reports, countries which are between the score range of 1.8-2.2 are those countries with problems of corruption suggesting that in these countries corruption is crucial and widespread.

There seem to be four basic problems of corruption in transition economies among the Central Asian countries (Detbier, 2003, p. 10):

- Autocratic structure owing to democratic problems in transition economies;
- Undeveloped market structure because of the powerful control of local elites;
- Weak governance;
- Local and regional conflicts causing problems in the nation-building process.

It is seen that economic shock therapy has led to corruption in the region along with the undeveloped economies in Central Asia. Countries in the region transformed their central planning economic system to a free market system in a very short period under the leadership of Washington-based Institutions. In Table 3 below, the economic freedom scores of the countries with respect to ten different liberties for the transformation of these countries are given in comparison to the world average.

Table 3

Economic Freedom Score of Countries

	Overall score	Business	Trade	Fiscal	Government expenditure	Monetary	Investment	Financial	Property rights	Corruption	Labor
Azerbaijan	58.8	75	77	80	77.5	63	55	40	20	19	83
Kazakhstan	61	74	86	88	82.1	66	30	50	30	22	83
Turkmenistan	42.5	30	79	90	94.7	63	0	10	10	18	30
Kyrgyzstan	61.3	77	76	93	80.2	62	50	50	25	18	83
Uzbekistan	47.5	68	65	88	72.6	62	10	10	20	18	61
Tajikistan	53	57	83	89	78	58	25	40	25	20	54

Note. Source: Statistics are compiled from the Heritage Foundation Economic Freedoms 2008 Data.

As regards the figures in Table 3, as a result of economic transformation in the Central Asian Turkish Republics, freedom in business has improved except in Turkmenistan. Freedom in business, trade and government expenditure have gradually improved. Freedom of labor in Turkmenistan is low compared to that in other countries. It is seen that liberties in these economics have improved in the direction of the IMF and the WB prescription. As seen in Table 3, the crucial problems of Central Asian Turkish Republics are with investment, property rights and corruption. Freedoms in the institutional improvements and the living standard of citizens have an important impact on these problems.

According to Table 4, income distribution is more balanced in those countries exporting natural resources except for Turkmenistan. The disconnection of poverty vs. GDP can be seen when Azerbaijan and Uzbekistan are compared. Countries seem to transfer some of natural resources rent for subsidizing the community with an

attempt to eliminate poverty. It is also possible to say that there is insufficient investment in comparison to its population in Uzbekistan, which has a level of GDP comparable to that of Azerbaijan.

Table 4

Social Indicators of Countries

	Population (million)	GDP (billion US \$)	Poverty rate (population) (%)	Health expenditure (GDP) (%)	Education expenditure (GDP) (%)	Military expenditure (GDP) (%)
Azerbaijan	8.4 (2005)	78 (2008)	< 2 (2005)	1 (2008)	2.6 (2008)	2.6
Kazakhstan	15 (2003)	175 (2007)	17.2 (2003)	2.3 (2007)	3.6 (2007)	1.2
Turkmenistan	6.5 (2005)	28 (2005)	n/a	4.8 (2005)	5.4 (2005)	n/a
Kyrgyzstan	5.1 (2004)	12 (2008)	51.9 (2004)	2.4 (2008)	5.2 (2008)	2.4
Uzbekistan	25.6 (2003)	72 (2007)	76.7 (2003)	2.4 (2007)	8.9 (2007)	0.5
Tajikistan	6.3 (2004)	13 (2008)	50.8 (2004)	1.2 (2008)	3.4 (2008)	2.1

Note. Source: The data have been compiled from the WB, the IMF and the EBRD data.

Social indicators in Central Asian countries such as education and health expenditures are behind the world average as a percentage value. It should be emphasized that there is a big gap between the world average and the Central Asian Turkish Republics. While Kazakhstan has a high level of per capita investment in education in comparison to the other countries in the Central Asian Turkish Republics, Tajikistan and Kyrgyzstan have the lowest level of investment in education (CIA, Factbook). Although military expenditures are seen to be high in proportion to the countries in problematic regions, in generally, it seems to need a high level of military expenditure but is not different than the other expenditures. Because the GDP figures are low in Central Asian Turkish Republics, it is not possible for these countries to focus just on military expenditures. Needing to improve their social structure, they give more emphasis on education and health expenditures

Conclusion

The fundamental problem of Central Asian Turkish Republics mainly depends on two facts: The first is the inequality of income distribution which leads to corruption; The second is the insufficient development of property rights caused by the failures of transformation of economic system. The main reason of economic underdevelopment in the countries exporting natural resources is corruption in sharing the rent of natural resources. It is essential to improve institutional structure for the solution of this vicious problem of corruption.

While the roots of institutional structure lean on the past, institutional structure is a way of thinking and a way of behavior which could convey communities to the future (Demir, 1996, p. 173). Therefore, it is crucial to implement those policies which could construct a stable institutional structure. The orthodoxy of Washington-based institutions have been implemented for the past 20 years during the transformation process of Central Asian Turkish Republics from the socialist system to capitalist market economy. As a consequence of the implementation of such orthodox policies, problems of institution-building occurred. In that sense, it could be argued that new economic concepts with new methods are required to solve such institutional problems.

The first handicap of institutional-building is problems concerning national identity-building owing to the political legacy of Soviet Union and the Russification process implemented during the Soviet Union. Unless a citizen is integrated to the nation-building process (in a country), the national economy fails to improve. The

second handicap is the drastic change in economy. The transformed economic system could be named as “limbo”, one between communism and capitalism, representing properties of both systems, thus making it difficult to integrate to the new system. As long as the old habits continue, they build up hindrances in the current system. The third handicap is the failure of an improvement in the legal system during the process of the economic transformation. Property rights, the fundamental element for social transformation, have a strong impact on resource distribution. It is strongly argued that legally protected “right to property” is crucial, as it leads to factors of production which generate economic development.

In order to solve the problems of Central Asian Turkish Republics, a legal structure with an institutional economic concept should be constructed instead of adopting neo-liberal economic policies. The weak governance, dysfunction of the legal system and undeveloped institutional economic structure result in a severe ethical problem in the society, which could only be solved by well-designed educational programs on national rights and duties for both bureaucrats and citizens. To strengthen governance and the legal system are especially required to regulate the property rights as the problems of these countries seem to be mostly institutional and moral rather than based on the freedom of labor and government expenditure. From a wider perspective, since the Central Asian Turkish Republics are in a region with a wide hinterland, the economic improvement of these countries could further support the economic development of Southeast Asian countries as a market.

References

- Altay, A. (2003). Economic roles and functions of government and small and medium sized organizations (SMSO) in transition economies. Istanbul University, *Conferences of Financial Research Centre*, No. 86.
- Demir, Ö. (1996). *Institutional economics*. Ankara: Vadi publications.
- Detbier, J. (2003). Corruption in the CIS-7 countries. *Lucerne Conference of the CIS-7 Initiative*.
- Gürbüz, S., & Dikmenli, O. (2009). Organizational perspective of corruption: An exploratory study in the context of its concept, its nature organizational environment, organizational behavior, and organizational architecture. *The Journal of Institute of Social Sciences*, 22.
- International Transparency Organization. (2001). Global corruption report. Data and research.
- NORAD. (2009). Anti-corruption approaches, a literature review. Study 2/2008, Evaluation Department, Norwegian Agency for Development Cooperation.
- Rock, M. T., & Heidi, B. (2004). The comparative politics of corruption: Accounting for the East Asian paradox in empirical studies of corruption, growth and investment. *World Development*, 32(6).
- Rodrik, D. (2006). Goodbye Washington consensus, hello washington confusion? A review of the World Bank's economic growth in the 1990s: Learning from a decade of reform. *Journal of Economic Literature*, 44(4).
- Stiglitz, J. (1998). More instruments and broader goals: Moving toward the post-washington consensus. The 1998 WIDER Annual Lecture, Helsinki, Finland.
- Williamson, J. (2000). What should world bank think about the Washington consensus? *The World Bank Observer*, 15(2).
- Williamson, J. (2003). Our agenda and the Washington consensus, in after the Washington consensus: Restarting growth and reform in Latin America. In P. Kuczynski, & J. Williamson (Eds.), *Washington: Institute of international economics*.
- World Bank. (2010). Introduction to corruption, module III. Retrieved from worldbank.org/etools/library/latestversion.asp?35970.
- Yüce, M. (2004). *The adaption problem of the Kyrgyz Republic in the free market system*. *The Journal of Industrial Relations & Human Resources*, 6(1).