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Uzbekistan, Central Asia's Poisoned Chalice

By Simon Speakman Cordall

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A couple of Uzbeks making their way down a rain-drenched street in Khiva, a desert town of 50,000 people. **Simon Speakman Cordall**

Last December, Uzbek President Islam Karimov officially designated 2013 as his country's Year of Prosperity and Well-Being at a ceremony meant to celebrate the 20th anniversary of the national constitution in the Uzbek capital, Tashkent.

The declaration was to have been the watershed moment when Uzbekistan opened its doors to foreign investment and welcomed international commerce to the resource-rich shores of the Central Asian state. Indeed, Uzinfoinvest, a state-owned enterprise aimed at fostering foreign investment, has made much play of Karimov's remarks, and his message has been echoed on the websites of Uzbek embassies the world over.

But some foreign investors are not buying into the rhetoric. And perhaps for good reason.

The Central Asian country is reaching out to foreign investors, but few are interested in taking the plunge.

In January, just a month after Karimov's speech, the Uzbek subsidiary of Russian mobile phone giant MTS filed for bankruptcy in the face of what it described as a government-sanctioned asset-grab.

"MTS Uzbekistan was the target of blatant harassment by Uzbek authorities with the thinly veiled purpose of destroying the business and expropriating its assets," said Irina Agarkova, a Moscow-based spokeswoman for MTS.

MTS, which is fighting back by suing the Uzbek government at the World Bank's International Center for Settling Investment Disputes, entered Uzbekistan in 2004 by acquiring a 74 percent stake in local operator Uzdunrobita for $121 million.

"MTS entered Uzbekistan with great optimism," Agarkova said by phone a few days ago.

Then in 2007, according to the terms of their agreement, MTS acquired the remaining 26 percent stake in Uzdunrobita for $250 million. Meanwhile, MTS also invested a further $1.1 billion into developing its nascent Uzbek operations, allowing it to deliver 2G, 3G and 4G services to more than 9.5 million subscribers — nearly 38 percent of the population of 28 million — by mid-2012.

But then Uzbek authorities began to open a series of investigations, impeding MTS' operations and leading to a $600 million fine that ultimately forced it to declare bankruptcy.

"MTS Uzbekistan and its employees were persecuted by Uzbek law enforcement authorities on the basis of unfounded accusations regarding tax, licensing and other alleged violations," Agarkova said.

Uzbek authorities, who are notoriously difficult to reach for comment, have made little public comment about the case. The Russian government suspects that two of MTS' rivals in Uzbekistan orchestrated the affair and is conducting its own investigation.

No matter who was at fault, the case dealt a body blow to Uzbekistan's efforts to attract foreign investment at the very time that the government was reaching out for capital.

The country has a lot to offer foreign investors, especially in terms of natural resources like oil and gas reserves but also uranium, gold and other mineral riches. Its location on the old Silk Road remains strategically and commercially important for regional transit transportation links. The workforce is also a potential draw, with the country boasting the largest population in Central Asia.

"In terms of competitive labor input, the country is in an advantageous position compared to its regional peers, having the largest population," said Lilit Gevorgyan, regional analyst at IHS Global Insight.

The government plays up these advantages as well as its efforts to improve the investment climate on the website of Uzinfoinvest, the foreign investment agency.

Uzinfoinvest boasts in a section of its website titled "Investment Policy of the Republic of Uzbekistan" that Uzbekistan's investment legislation is among the most advanced in the former Soviet Union. "It [has] incorporated major provisions of the international investment law, in particular regulations on guarantees of the rights of foreign investors [and] certain preferences for investors," it says.

However, despite its wealth of potential, Uzbekistan languors in the doldrums of global economic rankings, presently in 79th place, according to the United Nations.

Going some way to explain this fairly dismal performance are the experiences of foreign companies who have previously invested in Uzbekistan's promise. Unlike MTS, those operating in Uzbekistan were reluctant to describe their experience.

Danish brewing company Carlsberg, for one, has enjoyed mixed success since starting production in Uzbekistan in 2007 with a greenfield operation that created 300 jobs. After purchasing the production facilities of Sarbart Plus, a joint venture between the Uzbek government and the Baltic Brewing Company, Carlsberg invested a further $100 million into the business, only to have production halted in March last year following a tax dispute. Operations resumed in April of this year.

Ben Morton, Carlsberg's vice president of international media relations and issues management, kept his remarks brief and to the point when contacted by phone.

"We did temporarily suspend production, but we are now selling beer again," Morton said.

Carlsberg's circumspection is understandable. MTS' collapse continues to cast a long and threatening shadow over many foreign businesses operating within the region. As with much in Uzbekistan, the circumstances surrounding that exit are shrouded in suspicion and accusations of corruption at the highest level. Chief among the concerns aired since MTS' closure is the relationship between President Karimov's daughter, Gulnara, and Nordic telecom company TeliaSonera — a significant beneficiary of MTS' demise. Swedish television aired a report last fall that accused TeliaSonera of bribing top Uzbek officials, a charge that the company has denied.

Karimova, described in a leaked 2002 U.S. diplomatic cable as "the single most hated person in the country," is seen by observers as playing a key role in whether a major company succeeds or fails in Uzbekistan. "Most Uzbeks see Karimova as a greedy, power-hungry individual who uses her father to crush businesspeople or anyone else who stands in her way," the U.S. cable said.

Repeated requests for comment submitted to the Uzbek government and the president's office went unanswered over the past month.

MTS and Carlsberg's experiences are hardly unique. British company Oxus Gold, the Turkish-owned supermarket chain Demir and Indian textile giant Spentex also have faced conflicts with Uzbek officialdom, and the list goes on. In all cases, the suspicion of overwhelming state corruption is impossible to ignore.

"If you come to Uzbekistan, you will lose your money," said Steve Swerdlow, a Central Asia researcher at Human Rights Watch. "Businesses invest in joint ventures with the Uzbek government only to find themselves forced to sell out once they achieve profitability or simply be expropriated. The climate for business in Uzbekistan is like that for human rights: abysmal."

Last year, Time Magazine elevated Uzbekistan to sixth place on its list of the world's most corrupt countries in the world, up from 68th in 2002. A similar index by Berlin-based Transparency International ranked Uzbekistan in 170th place out of an overall 174 countries.

Gevorgyan, the analyst, said state protection of state officials for some domestic firms could provide them with privileges, including with tax and regulatory authorities, that distorts business competition. "This could be a serious obstacle for foreign businesses trying to find their way through Uzbek bureaucracy, which is perceived as highly corrupt both domestically and abroad," she said. "This is a particularly painful issue for foreign investors as again it affects market position and could lead to commercial losses."

Even one of Uzbekistan's competitive advantages — its workforce — has come under fire. Last month, the U.S. government downgraded Uzbekistan on its register of countries engaged in human trafficking following concerns over its use of forced labor.

"Over a million people, children and adults, are forced every year to leave their jobs and homes and work in the fields picking cotton, often for a pittance, sometimes for nothing," said Swerdlow, from Human Rights Watch.

His research has found that children from the age of 9 are forced to spend up to two and a half months of the year picking cotton on Uzbekistan's huge state farms. While theoretically outlawed in 2009, the practice remains a central pillar of Uzbek government policy, Swerdlow said.

"Forced labor is state-sponsored and government-controlled," he said. "Every year, Human Rights Watch receives hundreds of messages from those coerced into working on the farms. People are dying in the fields."

The Cotton Campaign, an NGO focused on the issue, describes the practice as follows: "Every year the government of Uzbekistan forcibly mobilizes over a million children, teachers, public servants and employees of private businesses for the manual harvesting of cotton. ... Profits of the Uzbek cotton sector support only the Karimov government. Uzbek farmers are forced to meet state-established cotton quotas, purchase inputs from one state-owned enterprise and sell the cotton to a state-owned enterprise at artificially low prices. The system traps farmers in poverty, and the state profits from high-priced sales to global buyers."

The United States and the EU are the primary destinations for much of Uzbekistan's cotton harvest.

Young cotton pickers are not the only employees who are suffering. Five MTS executives were imprisoned during the telecom giant's run-in with the Uzbek authorities. Oxus Gold's chief metallurgist, Said Ashurov, remains in prison on charges of espionage. Eight employees of Turkish retailer Turkuaz were convicted of tax evasion in 2011, and seven were summarily deported while one remains in prison. Meanwhile, Turkuaz, now under Uzbek ownership and renamed Toshkent, is said to be flourishing.

After his deportation, Turkuaz's former chief, Vahit Günes, said he was tortured during his nine and a half months in detention. "We were tortured badly using electric shocks. We saw people tortured to death; some of them had heads, hands and bodies dismembered," he told NBC Asia, a unit of the media development charity Institute for War and Peace Reporting.

GЯne? said he and the seven other jailed businessmen were forced to sign false confessions, ultimately leading to the expropriation of the retailer's $60 million in assets.

Accusations of torture have haunted Uzbekistan for years. The UN Office of the High Commissioner on Human Rights said in a 2009 report that torture and abuse by police and investigating authorities remain systemic, unpunished and are tacitly encouraged by senior government officials."

A former British ambassador to Uzbekistan, Craig Murray, has described in shocking detail the torture that he said he witnessed during his 2002-04 posting there.

"It means the woman who was raped with a broken bottle in both vagina and anus, and who died after 10 days of agony," he wrote in Britain's Independent newspaper in 2005. "It means the old man suspended by wrist shackles from the ceiling while his children were beaten to a pulp before his eyes. It means the man whose fingernails were pulled before his face was beaten and he was immersed to his armpits in boiling liquid. It means the 18-year-old whose knees and elbows were smashed, his hand immersed in boiling liquid until the skin came away and the flesh started to peel from the bone, before the back of his skull was stove in."

Murray was removed from his post as ambassador after publicly — and, observers said, rather undiplomatically — complaining about Uzbek human rights abuses.

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