

# The Shanghai Cooperation Organization, trade, and the roles of Iran, India and Pakistan

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*ABSTRACT This article seeks to explore the implications of Shanghai Cooperation Organization's (SCO) engagement with India, Pakistan and Iran. Not in terms of power-politics or as a counterbalance to the USA as this has been explored elsewhere, but what practical problems such an expanded organization could help solve, what opportunities it could realize, and how SCO's engagement in trade is a function of favourable political and bilateral developments in the region. It is argued here that the trade, infrastructure and energy sectors are of particular importance and that substantial potential gains could be realized if coordination is improved. Nevertheless, it is also recognized that China, Russia, Pakistan, India and Iran may have lower standards of democratic development and economic transparency than the West. What is the motivation behind the SCO's engagement with India, Pakistan and Iran? Should this engagement be conceived only in terms of balancing US unipolarity or are there legitimate concerns of increasing regional cooperation in Eurasia?*

## Introduction

The Shanghai Cooperation Organization (SCO) (consisting of China, Russia, Kazakhstan, Kyrgyzstan, Uzbekistan and Tajikistan) has attracted a significant amount of attention in recent years. Much of this attention is due to its potential role as a counterbalance to the USA in Asia and the SCO's increasing engagement with India, Pakistan and Iran, and extension of observer status to these countries in 2005 have made these worries even bigger. Even if the joint powers of China and Russia and their challenge to US interests in Eurasia has been a source of concern in itself the increased engagement with India, Pakistan and Iran in 2005 has exacerbated fears of an emerging anti-US bloc. It is to date uncertain if the

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permanent members of the organization will extend membership to the observer states but the mere fact that these Asian powers meet regularly without a US presence has made Washington wary of the ultimate ambitions of this organization. These concerns were not diminished with the SCO's call for the USA to vacate its bases in Central Asia at the Astana heads of state summit in 2005. What is the motivation behind the SCO's engagement with India, Pakistan and Iran? Should this engagement be conceived only in terms of balancing US unipolarity or are there legitimate concerns of increasing regional cooperation in Eurasia?

This article seeks to explore the implications of SCO's engagement with India, Pakistan and Iran. Not in terms of power-politics or as a counterbalance to the USA as this has been explored elsewhere, but what practical problems such an expanded organization could help solve, what opportunities it could realize, and how the SCO's engagement in trade is a function of favourable political developments in the region. It is argued here that the trade, infrastructure and energy sectors are of particular importance and that substantial potential gains could be realized if coordination is improved. Nevertheless, it is also recognized that China, Russia, Pakistan, India and Iran may have lower standards of democratic development and economic transparency than the West. A nuanced assessment of the SCO needs to recognize that this coordination will have both positive and negative effects for the West and will both complement and clash with Western interests of conflict prevention, democratization, and energy access.

There should be no doubt that the SCO is partly a vehicle for the permanent members and observers to justify and legitimize their own forms of domestic politics while providing a balance to US hegemony. Independent of this, however, there is a need to realize the benefits involved with increasing engagement across the East Asia/Central Asia/and South Asia divide. Such engagement could do much to make use of trade complementarities and poor interconnectedness in infrastructure across national and regional boundaries. Not to mention how greater interdependence could raise the costs of conflicts among the Eurasian states. Any development promoting increased regional dialogue about trade and other issues may promise to have conflict-preventive effects in this conflict-prone region. As argued by Johannes Linn and David Tiomkin,

... political and policy dialogue at the highest governmental level among the countries of Eurasia is important not least because it may help answer a key question about the future of cooperation and integration in Eurasia: will the unquestionable gains from economic integration and the increased interdependency, as well as a shared need for economic stability and prosperity among Eurasian countries drive increased political cooperation and peaceful coexistence in the region? Or will long-standing political tensions and new competition for scarce resources, especially for energy, create regional instability and divisions and, with this, serious barriers to the quick economic integration of Eurasia?<sup>1</sup>

This is how the SCO should be conceived and hopes should be kept realistic on the pace of integration. The SCO's move into the trade sphere should not primarily be assessed in terms of its ability to provide a regulatory multilateral framework of trade, similar to that of the European Union's common market or the North

Atlantic Free Trade Association, but as a way to coordinate and discuss such issues. Considering the growing complementarities between India, Pakistan and China on the one hand and Russia, Iran and the Central Asian states on the other in the energy sector, there is truly a need for a multilateral forum where energy infrastructure and trade and transit coordination may be discussed. The move of the SCO into the trade sphere and its engagement with Iran, India and Pakistan is a manifestation of the growing trading ties within Eurasia that has consolidated itself in the post-Cold War period. The expansion of SCO to include Iran, India and Pakistan, however, carries political costs and involves significant manoeuvring to be realized. This is unlikely to happen as long as internal conflicts and external pressure (mainly from the USA) continues. In addition, extending membership of SCO to India and Pakistan may also result in yet another conflict being brought into the organization. It is also hard to see how the SCO could provide a truly multilateral trade framework considering that all regional initiatives so far, e.g. the Economic Cooperation Organization (ECO) and the Eurasian Economic Community (Eurasec) have remained ineffective. The World Trade Organization will also be the main regulatory framework in trade between China, Pakistan and India and, as Russia is likely to accede soon, this will further undermine the rationale for other regional initiatives.

### **The SCO: from border disputes, to counterterrorism and trade**

The SCO was first initiated in 1996 as the Shanghai Five group consisting of China, Russia, Kazakhstan, Kyrgyzstan and Tajikistan to solve the disputes in the border areas and initiate confidence-building measures for this purpose. This was specified in the Agreement on Strengthening Mutual Trust in Military Fields in Border Areas in 1996 and the Agreement on Mutual Reduction of Military Forces in Border Areas in 1997. With the Almaty Declaration in 1998 it was agreed that the Shanghai Five would extend cooperation into combating ethnic separatism, religious fundamentalism, international terrorism, arms-smuggling, narcotics and other cross-border criminal activities. In 2000, Chinese President Jiang Zemin suggested that the up till then *ad hoc* nature of the Shanghai Five would be transformed into an institutionalized mechanism for multilateral cooperation. With the inclusion of Uzbekistan in 2001 the Shanghai Five officially became the SCO and this was followed with the establishment of a Secretariat and a Regional Anti-Terrorist Structure in 2004. In 2005, Iran, India and Pakistan became observers to the organization whereas Mongolia was granted observer status a year earlier.

In the summer of 2006 the member states of the SCO gathered in Shanghai to celebrate the five-year anniversary of the organization. Although the Shanghai Five (and the SCO) initially emerged as an organization primarily occupied with the settlement of border disputes and counter-terrorism it has lately devoted efforts to trade facilitation. The idea of economic cooperation and trade facilitation efforts surfaced already in the 1990s within the framework of the Shanghai Five but it was only with the launch of the SCO in 2001 and the establishment of a Secretariat

that the initiative started to gain currency. That year the SCO members signed a memorandum of understanding on regional economic cooperation that was to be followed by the adoption of the Multilateral Trade and Development Program in 2003. The programme was subsequently specified in more detail at the Tashkent summit in 2004 where 127 projects were included in a specific regional action plan. Of these, 19 were related to energy cooperation, 20 to transport cooperation and one third to cooperation in the spheres of education, science and technology.<sup>2</sup> The same year China also announced its provision of a US\$900 million grant in export credits for the Central Asian countries to jump-start the programme. The programme was finally implemented at the Moscow heads of government summit in the fall of 2005, and the institutionalization of the SCO Inter-Bank cooperation and the SCO Business Council is currently gaining momentum. The Inter-Bank cooperation will facilitate bank transactions and bank access for traders in third countries and smooth foreign investments, while the Business Council is set up to assist dialogue among the largest companies in the region; this is also something which entrepreneurs in the region have identified as main impediments to further investments.<sup>3</sup> This move into the trade sphere coincides with one of the most significant contemporary developments in the global economy; the re-integration of economies located along the Silk Road and increasing trade ties between China, India, Russia, Pakistan, Iran, Azerbaijan and the Central Asian countries. Transport corridors from Central Asia down to the Indian Ocean via Afghanistan are being restored, and overland trade from China via Central and the Caucasus to Europe is increasingly becoming a viable alternative.

### **The rationale for a greater regional dialogue**

These trade routes also have a long history. Through the Kuchan, Roman, and Persian empires trade have been conducted from the Indian Ocean stretching as an arc from the Rimland of the Indus basin to the Heartland of Central Asia. Rulers from Central Asia in the Moghuls, Tamerlane, and Mahmud of Ghazni have all controlled India's northwest and shaped its culture.<sup>4</sup> What today stretches up north of the Pamir mountains, into the Fergana Valley, to Khorgos in the East and the Caspian in the West was a zone of strong economic interaction which may see its economic revival today as walls of protectionism and self-sufficiency are torn down. During Soviet time cross-border interaction and trade between Central Asia, Afghanistan, China, and Iran were minimal. In addition, before Deng Xiaoping's leadership in the 1970s and the opening up of the Chinese economy, China's foreign trade was similarly limited and the same applies to the period of Nehruvian socialism in India and Iranian populism under Khomeini. A century of almost constant instability and conflict in Afghanistan, more than 50 years of conflict between India and Pakistan, the end of the Shah-era in Iran, and border disputes in the entire Eurasian region have had detrimental effects for these economies.

The disintegration of the Soviet Union, the 'normalization' of Indo-Pak relations (despite recent drawbacks), the death of Khomeini, and Indian

integration into the world economy have however significantly altered the opportunities for cross-border trade in Greater Central Asia and with its neighbours. Trade potential between China, Afghanistan, India, Pakistan and Iran, the five Central Asian nations, and all the way to Western Europe is considerable. These potentials involved in continental rather than regional trade in Eurasia is best viewed in context of that the traditional Eurasian sub-regional trading blocs (Asia Minor, China, Commonwealth of Independent States (CIS), East and South-east Asia, Europe, Japan and South Asia) are today trading more with other blocs than within the blocs and intra-bloc trade amounts to no more than approximately 20 per cent in all blocs, with the exception of Europe.<sup>5</sup> A major driver for this is growing energy needs in India, Pakistan, China and enormous energy supplies in the Caspian, the Middle East, Central Asia and Russia have also led to significant complementarity between the Eurasian economies. The same applies to the textile industry where Central Asian cotton may find new and emerging markets in India and Pakistan. Natural specialization could be achieved by opening old trade routes and encouraging greater inter-state cooperation: China tapping into Central Asian energy resources and Kyrgyzstan has taken steps to supply Afghanistan with building materials. Cotton from Tajikistan and Uzbekistan could be exported to China, India and Pakistan, Pakistani producers could compete with Chinese and Indian manufacturers, and China could provide Central Asia and Russia with technology and manufactures.

With the end of the Khomeini era and the opening up of the Iranian economy the Chinese became interested in further engagement, especially as energy slowly became an issue in China. In 1992 China's railway ministry signed a memorandum on cooperating in the establishment of new railway lines connecting the Central Asian with the Iranian railway lines. In May 1996 the Mashhad–Tejen railway connection opened, running between Iran and Turkmenistan, making further transportation through Central Asia and Xinjiang possible. During the 1990s and early 2000s further efforts were also devoted by the Chinese and Iranians to greater interconnectivity in the railway sector. Today, China is engaged in constructing a new railway line from its Pakistani port in Gwadar to link with the Zahadan-Quetta railway line running between Iran and Pakistan.<sup>6</sup> Even if the economies of the current SCO members are already complementary, the inclusion of Iran, India and Pakistan into a greater dialogue would increase the ability to discuss matters of concern south of the former Soviet border.

Such dialogues are also markedly absent today. The SCO has however started to realize these potentials that have opened. As the SCO Secretary General Zhang Deguang recently noted: 'The most serious challenge to the SCO in the next five years will be whether its cooperation in the field of economy can bring about important practical results and whether it can have a positive tangible effect on member states'.<sup>7</sup> In the main, however, the Eurasian states have been slow to adapt and realize potential gains. A major factor for this is the geo-political aspect and competition between the Eurasian states over territory, economy, and natural resources. This is unfortunate as it is exactly in trade between East Asia/Central Asia and South Asia where the potentials really are found; most obviously

in energy, but also in other sectors. For example, in 2005 bilateral trade between China and the five other SCO members reached almost US\$38 billion, up 212% from the launch of the organization.<sup>8</sup> Russia's trade with the other SCO members increased from US\$26 billion in 2001 to more than US\$41 billion in 2005.<sup>9</sup> Yet India's and Pakistan's total trade with Central Asia remains almost nonexistent making up less than 1 per cent of both countries' foreign trade despite substantial trade complementarity and geographical proximity.

The SCO could potentially play a significant role in furthering this development. That the economies of the present SCO member states are complementary in nature is best illustrated by the expanding trade volumes between the countries. Russia's overall trade volume with, for example, Kazakhstan, has grown steadily from approximately US\$3.8 billion in 1998 to US\$4.8 billion in 2001 and to top US\$8.1 billion in 2004. Moreover, according to Chinese Customs Statistics the total trade volume between China and Central Asia has increased from approximately US\$465 million in 1992 to US\$7.7 billion in 2005. In 2002, for instance, total trade volume reached a modest US\$2.4 billion, while 2003 saw an increase to US\$4.1 billion. The 2004 figure of US\$5.8 billion then increased by 72.5 per cent to an all-time high of US\$7.7 billion. The bilateral trade between China and Russia has seen a similar increase reaching more than US\$33 billion in 2006.<sup>10</sup> The energy-hungry economies of India and Pakistan and the Iranian energy supply are also likely to increase complementarities, but there is also a need to be realistic and see that many of these states also lack complementarities. Iran and Central Asia for instance are both in need of capital, energy-exports, contact with international business and strong private sectors rather than pursuing bilateral trade.<sup>11</sup> Moreover, a major problem in carrying out trade facilitation is that the SCO's trade programme operates on an *ad hoc* basis providing no permanent body devoted to these efforts. To date, trade, energy and economic matters are mostly settled bilaterally on the sidelines of the heads of states summits and the regional coordination aspect is often neglected. Paradoxically, the bulk of these deals seem to be between SCO members and observers, primarily between China and Russia on the one hand and India, Pakistan and Iran on the other. This indicates that a greater regional dialogue including not only China, Russia and Central Asia, but also its neighbours in South Asia is long overdue.

### **SCO's Multilateral Trade and Development Program and economic engagement**

With the further entrenchment of the Multilateral Trade and Development Program, the eventual institutionalization of a staffed permanent body, greater interaction with its observers, SCO promises however to fill perhaps one of the most important functions in Eurasia—rehabilitation of infrastructure, increased interaction in the business and banking sectors, energy cooperation and bridging the South and Central Asia divide. Unfortunately the SCO's trade programme currently lacks a regional strategy for trade facilitation. Although the economies of the SCO member states are booming with official growth rates pending

between 5 and 10 per cent for all states, there is great need for further efforts to take full advantage of the potentials that have opened. The recent five-year anniversary summit in Shanghai gave some initial promises for this, even though trade and infrastructure coordination still is in its infancy. The agenda of the summit primarily included development of railways and motorways, communications and information systems, as well as the implementation of the SCO Business Council. Within the framework of the SCO interbank cooperation, an agreement to finance US\$500 million worth of Russian–Chinese projects in energy, agriculture and investment projects between Vnesheconombank and the State Development Bank of China was reached.<sup>12</sup> A total of US\$2 billion worth of contracts were signed during the summit between the SCO members and observer states—yet most of these were made bilaterally rather than under multilateral supervision. Here, deals between Iran–India and Iran–China in developing the Yadavaran oil field in Iran as well as Iranian supply of liquefied natural gas to China and India were dominating bilateral talks.<sup>13</sup> The Indian Minister of Petroleum and Natural Gas Murli Deora also stated after the summit that a dialogue on the Iran–India–Pakistan pipeline had been held and that it was progressing on ‘fast track’.<sup>14</sup> China and Kazakhstan signed two documents during the summit on the construction of the Moynak hydro-electric power station as well as the renewal of a passenger rolling stock in Kazakhstan. Discussions on the proposed natural gas pipeline from Iran, via Turkmenistan, Kazakhstan to China were also reported to have taken place between the respective heads of states.<sup>15</sup>

Perhaps most significant was however the announcement that Chinese state oil company Sinopec is buying TNK–BP’s 96.9 per cent share of Russian Udmurtneft worth approximately US\$3 billion. As this deal has now been finalized this represents a further step in the right direction in these countries’ bilateral energy cooperation.<sup>16</sup> A first sign that the strategic aspect of the Sino–Russian energy relationship is abating slightly was also seen in 2004 when Chinese banks financed Rosneft’s acquisition of Yuganskneftegaz with a US\$6 billion loan.<sup>17</sup> These cases should however be considered as exceptions rather than rule. In total, China is so far dissatisfied with the pace of Russia’s concessions in the energy sector. This was also revealed by the vice-director of China’s National Development and Reform Commission, Zhang Guobao in a recent interview with Interfax where he stated that Russia had complied with commitments on oil exports by rail to China, but as for cooperation in other areas, there had been a lot of contact and communication, but ‘little actual progress’.<sup>18</sup>

Despite the strategic aspect of energy coordination, infrastructure restoration and trade facilitation, there is significant room for regional coordination. In the main, the SCO currently provides a forum for fortifying bilateral deals, at least between SCO members and observers, rather than regional cooperation coordinating shared interests.<sup>19</sup> This is unfortunate as greater regional coordination and more extensive involvement of India, Pakistan and Iran would increase efficiency and reduce collective action problems. This will also mean more options and outlets to the world market for Central Asia—something which truly is in the interests of these states. Competition will boost productive efficiency, minimize

welfare losses and make transport across the Eurasian continent become an option. The key component for this to materialize is however the presence of political will. Russia has been trying to maintain the Central Asian states within its orbit and China has been reluctant in letting additional states into their strategic interests in Central Asia. As long as China and Russia deny and actively work against Central Asia's access to South Asia it will significantly impede Central Asia's realization of potential gains. Moreover, as long as states in Eurasia are stuck in old thinking and view the regional economics as a zero-sum game, coordination will be hard to achieve.

### **Principal challenge to SCO expansion: internal conflicts and external pressure**

Indeed, considering the complex relations among all these Eurasian powers, long-standing bilateral conflicts and contradictory alliances, more conflicts will be brought to the negotiation table in the event of SCO enlargement. Judging by the experiences of the South Asian Association for Regional Cooperation (SAARC) where the conflict between India and Pakistan has brought the entire organization into deadlock, both China and Russia will probably think twice before admitting these countries, especially as the Central Asian member states have the destabilizing effect of Pakistan's support of the Taliban fresh in mind.

The animosity between India and China does not facilitate things either. Although bilateral relations have improved markedly since the 1962 Sino-Indian War, tensions still exist. Here India's active lobbying for keeping China out of SAARC may affect China's whole-hearted embrace of India's membership in SCO.<sup>20</sup> China's aggressive development of infrastructure in Central, Southwest and South Asia is also feared in Indian policy-making circles to be a Chinese strategic encirclement of the South Asian subcontinent.<sup>21</sup> Of particular worry is that the Chinese will have a foot in the Indian Ocean as the Gwadar port opens,<sup>22</sup> and India has already launched its countermove by investing substantial sums of money in the competing Iranian port of Chah Bahar.<sup>23</sup>

Considering the strategic interests involved in such projects it seems that these states will find it difficult to cooperate in infrastructural development within the SCO. Fierce competition over 'competing' infrastructure is not confined to China and India solely but is pervasive on the entire continent. For example, the second Euro-Asia land bridge running east-west from China to Europe via Xinjiang will compete with the first Euro-Asia land bridge running on the trans-Siberian railway. The former is heavily promoted by China, the latter by Russia. Similarly, development of the north-south route from Central Asia via Afghanistan to the Indian Ocean will compete with the corridor running from India, via Iran, the Caucasus, and up to Russia. Within the energy sector it may also seem illogical why China and Russia would give a *carte blanche* to India and Pakistan to participate in the competition over Central Asian energy resources.

Even relationships that seem overall healthy have underlying conflicts affecting prospects of bilateralism and multilateralism. For example, the Russo-Iranian



alliance is almost completely confined to trade and armament cooperation and disagreements over the sectoral division of the Caspian Sea continue to haunt further cooperation, and Iran has certainly not forgotten Pakistani support of the Taliban during the 1990s, either of which may bring an additional conflict into the SCO.<sup>24</sup> Yet among all the conflicts plaguing the Eurasian continent the hostility between India and Pakistan stands out as the most serious obstacle to a greater regional dialogue including all these actors. Despite the rapprochement since 2004 there are no assurances that this engagement will be lasting, not least today when the Pakistani leadership looks increasingly fragile and has little control over the radical Islamism in the country.

Concern over relations with the USA is also limiting India's participation within the framework of the SCO. Carrots from the USA in assisting India with civilian nuclear technology as well as repeated statements of the bloc-like nature of the SCO from the USA is hindering a more extensive Indian participation in SCO. Signs of this cautious approach to the SCO from the Indian side are increasingly seen. The Indian leadership rarely makes statements on intention to join the SCO. In addition, as Indian Premier Manmohan Singh went to Russia in early 2006 and rumours surfaced that India was to take part with Russia and China in the SCO military exercises taking place in 2007, Singh was quick to reject these claims. The political costs of such participation are evidently too high.

Furthermore, following the controversies involved with Iran's participation and the present US–Indian engagement in civilian nuclear technology, India chose to be represented not by Prime Minister Manmohan Singh but by the Oil and Natural Gas Minister Murli Deora. This was most likely, again, due to the political costs involved.<sup>25</sup> While paying lip-service to the USA in not being represented at the heads of state level, India's balancing act between the USA on the one hand, and the SCO members on the other, may compromise the SCO's ability to entrench a system of multilateral cooperation including South Asia, not to mention that India's reluctance in further engagement will undermine Pakistan's as well as Iran's intentions in joining the organization. Considering the current power configuration within the SCO, with the Sino–Pakistani alliance on the one hand, and the Russian–Indian alliance on the other, Singh's absence signifies more than just an unconvinced India. With India being reluctant about further engagement with the SCO, Russia would never allow the increased Pakistani engagement promoted by China. With India and Pakistan remaining outside of the organization this inadvertently will affect China's and Russia's position on Iran's membership. Considering the fact that a single accession of Iran without being followed by India and Pakistan would undermine the legitimacy of the entire organization as a result of the symbolism involved, there are hardly any factors that would make the SCO take such a risk.

This risk was made evidently clear both ahead of the recent SCO summit in June 2006 and afterwards, where a main concern of USA policy-making circles and media was the invitation of Iranian President Ahmadinejad.<sup>26</sup> Former US Defense Secretary Donald Rumsfeld was quoted as saying before the summit that: 'It strikes me as passing strange that one would want to bring into an

organization that says it is against terrorism one of the leading terrorist nations in the world: Iran'.<sup>27</sup> Although the USA has concerns over Iran's participation in the summit and its influence on Iran's nuclear ambitions and relations with Russia and China, Iran's observer status and its influence in the organization should not be overestimated. Rarely is any attention given to the simple fact that the SCO member states have not granted Iran full membership, despite persistent requests from the Iranian side.<sup>28</sup> It should also be acknowledged that Iran is an observer to other international organizations where Iran has interests as well, most notably the World Trade Organization. The Iranian President was reportedly also asked by the other SCO member states before his address at the summit to concentrate on 'the problems of Shanghai Cooperation Organization' only, and was given 5 minutes only for this purpose.<sup>29</sup> Thus, the extent of Iran's current participation in the SCO should rather be seen as Russia and China giving in to US pressures rather than the opposite—an openly confrontational Sino–Russian–Iranian *entente* in Central Asia, especially as both China and Russia have great business interests and important security cooperation with Iran.

Another problem is that participation of India, Pakistan and Iran within the sphere of anti-terrorism would not work in the current circumstances. Frequent Indian accusations of ISI-sponsored terrorism across the line-of-control and Pakistani allegations of Indian state-terrorism and human rights violations within Jammu and Kashmir would make the SCO Regional Anti-Terrorist Structure impossible to manage. The fact that China has convinced some of the other SCO members to extradite their own Muslim Uighur citizens to China would provoke resentment in Iran and Pakistan over participation in such activities as well. Apart from cooperation in the trafficking of drugs and migration there are few sectors within the security sphere where all of these could reach a consensus today. All in all, there should be no doubt that all these factors will pose major difficulties in initiating a dialogue among all these states.

### **Reasons why these states should be able to overcome these problems**

Yet the fact that China, Russia and the Central Asian states actually do cooperate is, however, a sign that conflicting of interests may be temporarily relinquished within the framework of SCO cooperation. This is a major achievement. Despite fierce competition in the energy sector, Chinese expansion into the Russian Far East<sup>30</sup> and a Russia that as late as 2002 allied with the USA rather than China, they have been able to shelve these issues for the present time. The major question is however whether this would be the situation with India, Pakistan and Iran's inclusion as well.

Evidence so far suggests however that even the most dissimilar states have been able to overcome political differences and strains while seeing the pure economic rationality in cooperating. Iran and China, and India and China are two cases in point where bilateral trade has exploded despite deep-rooted conflicts and/or conflicting ideologies. Bilateral trade volume between China and India has grown from US\$200 million in the early 1990s to almost US\$20 billion in 2005.<sup>31</sup>

Simultaneously China is expanding trading ties and making progress on the border disputes with India, where the agreement signed in June 2006 to reopen the trade route at the Nathu La pass in the Himalayas that has been closed since the Sino–Indian war in 1962 is a breakthrough event. Some realist assessments view the Sino–Indian rapprochement with suspicion and that the Chinese push for development of transport links to South, Southeast and Central Asia will be met with fierce rivalry from India.<sup>32</sup> Even so, both India’s and China’s ‘competition’ in investing in regional infrastructure will benefit the regional economy and individual countries substantially as transport times are shortened and transaction costs reduced.

Thus cooperation in the economic sector seems to be possible as long as the states involved realize the potential gains. All countries in the region also face the same problem—sustain growth or face political instability. To sustain growth there is need for a rapid development of infrastructure, as well as interconnections of these to neighbouring states. The extent to which policy-makers in the concerned states realize this will also determine the scope of cooperation.

Second, arguments that the SCO may face the same fate as the SAARC if India and Pakistan is admitted are to some degree valid. There are however some differences between these two cases that should be raised. The problem with the SAARC has been that India’s absence has postponed the heads of state summits, which has essentially placed the whole organization in stalemate. A SAARC summit without India would not have much legitimacy considering the weight of that country. In contrast to the SAARC where the absence of India and Pakistan undermines the objective of the entire organization, the SCO can have fruitful deliberations even if India and Pakistan do boycott the summit. There is no legal impediment specified in the Charter for holding the summit in the absence of a member state, nor is there any provision in the Charter that all states need to be present to take decisions.<sup>33</sup> Also, should the conflict between India and Pakistan be brought into the organization the original members may also exclude them for ‘violating the provisions of this [the] Charter and/or systematically failing to meet its obligations’ as specified in Article 13 of the SCO Charter.<sup>34</sup>

In sum, with the granting of membership being reversible if repeated violations of the Charter occur and the organization being able to meet and take decisions even in the absence of any member state or states, India, Pakistan (or Iran) cannot ‘hijack’ the organization in a similar way as has happened with the SAARC. Should either of the new members veto or raise their objections to each decision taken the SCO could also exclude them for ‘violating the provisions of the Charter’, which contravenes SCO member’s obligations to ‘encourage the efficient regional cooperation’ (Article 1). Yet, even though the current SCO member states realize that they always have this option, this does not necessarily mean that they would take the risk. Currently, this seems to be the case and this is a major problem for expansion, not to mention the fact that the regulatory framework and Charter of the SCO may be as weak as in the other Eurasian organizations (e.g. the CIS Charter and associated documents).

**Other benefits in cooperation: confidence building, security and conflict prevention**

Should these obstacles be surmounted, benefits other than regional cooperation and trade will accrue, especially with regards to confidence building and conflict prevention in Eurasia. For the first time since partition of British India in 1947 into India and Pakistan (India, Pakistan and Bangladesh in 1971) the intrinsic interdependence between India on the one hand, and the states of Afghanistan, Pakistan, Iran, Central Asia, China and Southeast Asia on the other seems to be restored. Confidence-building measures between India and Pakistan across the line-of-control in Jammu and Kashmir have increased, even if there has been a serious stalemate after the bombings in India in 2006. Even if the conflict is far from resolved, increased interaction in the movement of people and goods between India and Pakistan promises incremental progress to a viable peace. In addition, although conditions in Afghanistan have deteriorated in 2006/2007 affecting ties between South and Central Asia negatively, this makes it even more important to include Afghanistan into the regional economy, not least for the former post-Soviet states. If this could be achieved, this would mean increased access to ports in Pakistan at Gwadar and Iran at Bandar Abbas and Chah Bahar for Central Asia giving important outlets for products to the world market. India and Pakistan will also get a further source of energy and an important diversification away from a reliance on the Middle East. Should the security situation in the Pakistani port of Gwadar deteriorate further and jeopardize the entire project, which some argue is happening,<sup>35</sup> the Iranian ports of Chah Bahar and Bandar Abbas will increase in importance for the Central Asian states and Afghanistan. Earlier on, the Iranian Shiites' distaste for the Taliban and its concern of the Karzai government's staying in power was also an area where the interests of Iran and the US coincided. This applies to China's and Russia's interests as well.<sup>36</sup>

Moreover, for the first time since the 1960s China has shown a more moderate and objective position in the conflict between India and Pakistan. Although China still is, and has been, Pakistan's staunchest supporter in the last 50 years, ties between China and India are improving. China's more cautious approach to the authority of the United Nations' (UN) resolutions on Kashmir and hesitancy in supporting Pakistan in the Kargil conflict with India in 1999 are breakthrough events in the trilateral relationship. The continuous Chinese support of Pakistani intrusions across the line-of-control has also for the first time seen signs of abating.<sup>37</sup>

In addition, the SCO will face significant problems in tackling both security challenges and trade opportunities if Afghanistan is not further engaged with the organization. The anti-drug belt that the SCO has launched in response to the booming poppy cultivation will not make any major achievements if this is not coordinated with the Afghan government. Trade facilitation efforts in Afghanistan are today carried out mainly by Japan, the USA and Asian Development Bank (ADB) in cooperation with the Afghan government. In order for the SCO to be credible and comprehensive Afghanistan's participation is vital.

An SCO–Afghanistan Contact Group has been established but the scope of activities within this framework is so far limited. As the successful restoration and reconstruction of Afghan society and infrastructure is a key component in a dynamic South and Central Asian market, Afghanistan needs to be further integrated into the SCO structure. The main obstacle here is the close ties between Hamid Karzai’s government and the USA, which will prevent any closer engagement with the SCO. Indeed the present set up of cooperation in the Contact Group seems to be a middle ground for Afghanistan and the SCO pursuing their interests while still maintaining good ties with the USA.

Security threats of terrorism and drug-trafficking emanating from Afghanistan are also destabilizing and affecting all SCO members adversely. Traffickers have shifted towards the northern route via Central Asia and Russia as a result of greater efficiency among Iranian border authorities on the southern route and China is increasingly facing a problem with drugs entering the country through the Wakhan corridor or via Central Asia.<sup>38</sup> Secure border regimes and reduced incentives for extremism are the leitmotifs of both the SCO and the USA in the region and there is a need for both parties to recognize the complementary rather than competitive elements here, not to mention that this will be a fundamental precondition for economic development and trade.

### **Problems and opportunities: a balance sheet for the USA and Europe**

What then are the likely negative implications for Western interests in the region of this increased engagement within Eurasia? Assuming that the overarching interests of the West in Eurasia is democratic development, the development of transparent market economies, energy access and stability, the harmonization of interests in Eurasia have both its pros and cons. The major benefits that will accrue Western interests were mentioned above. These pertain particularly to increasing interdependence, trade-led growth, confidence-building and conflict prevention. This is not to say that conflicts will not erupt but in the event they do they will be far more costly for the parties involved. On the negative side, the most obvious challenge to US and European interests is in terms of balance of power. These states may raise their bargaining positions *vis-à-vis* the West when speaking in concert: the role of Iran’s and North Korea’s nuclear programmes being two cases in point. It should also be acknowledged that it would be wrong to assume that the SCO is a ‘neutral’ organization without any agenda besides promoting all of its members’ interests. The fact that the SCO is a China-initiated and China-dominated organization should also be taken into consideration when assessing the SCO’s future role.<sup>39</sup> Chinese interests may change and it would as such be wrong to assume that the SCO’s *raison d’être* is fixed.

Second, given that arms transfers makes up a large portion of the trade between China and Pakistan, Russia and India, Iran and Russia, and China and Russia this may pose significant challenges to US interests in the long term as these states’ scientific competencies, technological know-how and economic growth promote defence modernization.

Third, although the US isolation of Iran has done much to harm the Iranian economy and investments into Iran's energy sector, the increasing engagement with China, Russia and India has provided it with other sources of import and export. Even if the USA has enough leverage to prevent India from engaging Iran, as has been seen in the paused Iran–Pakistan–India pipeline project, the USA does not enjoy this amount of leverage on either China or Russia.

Fourth, as has been seen elsewhere (e.g. in Africa) the Asian powers' bilateral aid is driven more by promoting their own self-interest than raising poverty levels, democratic development and transparent market economies. In what has been described as 'rogue aid' this development aid to infrastructure and other social services may in fact compete with the aid provided by Western donors and the international financial institutions. In choosing between the World Bank who puts higher demands and sometimes have higher interest rates than states like China, the choice is quite straightforward. The SCO may also work as a vehicle to gain legitimacy on the international stage and as a method of evading international pressures for reform. The SCO's observer status in the UN General Assembly is one example of this.

## Conclusions

While it is tempting to explain the ambitions of the SCO and its interested observer states in terms of balance of power alone, this often overlooks the fact that the organization is more than an expression of power politics. A main reason why the SCO is engaging with Iran, India and Pakistan is due to favourable political and bilateral developments in Eurasia in the past 15 years and the fact that these states have legitimate concerns about coordinating trade and infrastructure developments. Increased interactions across Eurasia in all directions promise to further the potentials of these states to find new markets and Central Asia will find itself in the middle of this trade network. This is not to say that these burgeoning engagements in Eurasia do not pose challenges to Western interests. But the benefits should also be recognized. The increased interdependence and regional cooperation in Eurasia will raise the costs of conflicts and hopefully provide a climate conducive to entrepreneurship and cross-border interactions, which in the end will benefit Western firms as well. Expectations of a rapid institutionalization of a working multilateral regulatory trade framework should however be tempered. The SCO should rather be assessed for what it has accomplished thus far and how it is an effect of the growing ties and interdependence within Eurasia.

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