

KASHMIR

THE ECONOMICS OF PEACE BUILDING

A Report of the CSIS South Asia Program
with the Kashmir Study Group

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Photo Credit

Climber and Sherpas on Nun Kun
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Contents

List of Illustrations	iv
Preface and Acknowledgments	v
Introduction and Executive Summary	vii
Chapter 1: What Is Kashmir?	1
Chapter 2: The Indian Side: An Economic Snapshot of Jammu and Kashmir	9
Chapter 3: The Pakistani Side: Azad Kashmir and the Northern Areas	29
Chapter 4: Recommendations	45
About the Author	68
About the Kashmir Study Group	68

List of Illustrations

Jammu and Kashmir: Reference Map	xiv
Demographic and Economic Profile by Region	6
Jammu and Kashmir: Transportation and Drainage	8
Jammu and Kashmir: Distribution of Total, Urban and Rural Population and Population Density; Areas Most Affected by Earthquake of October 2005	44

Preface and Acknowledgments

The inspiration for this report, and the resources that made it possible, came from Farooq Kathwari. A dedicated son of Kashmir and a passionate believer in the American dream, Farooq asked CSIS, together with the Kashmir Study Group that he had founded in 1997, to take a hard and creative look at the economic side of peacemaking in Kashmir. Without his vision and support we could not have carried out this project; without his ideas, it would have been much poorer. He has had my friendship for 20 years. He has my profound thanks as well.

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My colleagues in the Kashmir Study Group listened patiently to an early draft of this report and provided invaluable feedback. Joseph Schwartzberg went through several drafts, which were much improved by his careful attention. Philip Schwartzberg prepared the maps in this study.

My small office at CSIS has assembled a remarkable number of talented and dedicated people whose contribution to the project was tremendous. Mandavi Mehta, who had just completed two years as my right hand and research associate, spent a week in J&K and helped me find some key sources of basic economic information. Pramit Mitra, her successor and my close colleague at CSIS, has kept the program humming. And among the interns who have volunteered in our program, I am especially grateful to Bidisha Biswas, Santosh Sagar, Bushra Asif, Maha Qazi, Bethany Tindall, Joseph Puthenveetil, and Divyesh Lalloobhai.

Whatever insights this report is able to provide owe a great deal to all these people—and to the many others with whom we spoke in the course of this project. The errors that remain are mine alone.

Introduction and Executive Summary

The Kashmir problem is the most intractable part of the dispute between India and Pakistan. In the past five decades, scholars and statesmen have analyzed the political dimensions of the problem many times over and have tried to solve it or at least to manage it. The economic dimensions of the problem have received much less attention.

Kashmir today is reeling under the impact of an earthquake measuring 7.6 on the Richter scale, with its epicenter between the capital of the Pakistani side of Kashmir and the Line of Control (LOC). It has left some 70,000 dead, even more wounded, and an estimated 3 million homeless facing the Himalayan winter. This report does not attempt to make a detailed assessment of the relief and reconstruction needs of the region; others are better equipped for that task. We have, however, reflected in this report some of the most urgent requirements for rebuilding infrastructure and some of the key opportunities for bringing Kashmiris from both sides of the line together in a rebuilding effort.

The lesson of the first anxious days following the earthquake is clear, however. This is a time for decisive action and a bold vision for a better future in Kashmir. We urge those who are frustrated with over half a century of stalemate in Kashmir to think big, both about new ways of responding to a tragedy and, more importantly, about finding a new and more cooperative model for bringing both economic life and political hope to a region that has had too little of either. The report's recommendations should be read in that spirit.

This study is an effort to address the lack of economic content in thinking on Kashmir. Starting from an assessment of the current economic picture in Kashmir, both the parts administered by India and those administered by Pakistan, it will attempt to define how economics might help to build peace. It will look at two levels:

- In the near term, measures that could be taken in the absence of major political change to build up peace constituencies and lay the groundwork for a peaceful future; and
- In the longer term, measures that could reinforce a long-term settlement and leave a more prosperous Kashmir integrated with the regional and world economies.

The study presents a long list of recommendations, a kind of cafeteria from which policymakers can draw, some capable of implementation by one side acting alone, others requiring joint action. All, however, could be implemented under a

variety of political arrangements. They draw on Kashmir's natural resources and its skillful, entrepreneurial population, and they attempt to steer clear of the problems created by long-term violence. Some initiatives would also require the participation of nongovernmental organizations and civil society. None should be read as a hidden appeal for any particular design of a settlement.

Economic interventions are not a substitute for fundamental political decisions or for the long and complex process of changing political behavior. Our hope in presenting this report is that policymakers will find in it economic tools that can facilitate the political changes that people in the region so badly need.

The Kashmiri Economies

Kashmir includes five different regions. Since the end of the war that followed the independence of India and Pakistan, three parts of the former princely state of Jammu and Kashmir have been under Indian administration: the Kashmir region itself (including the Valley of Kashmir), with a predominantly Muslim population, regarded by all parties as the heart of both the region and the problem; Jammu, south of Kashmir, with a Hindu majority; and Ladakh, a sparsely populated high mountain plateau area east of Kashmir proper. Two have been administered by Pakistan: Azad Kashmir, a thin strip between Kashmir proper and the Pakistani province of Punjab; and the Northern Areas, another mountainous and sparsely settled area. Both are entirely Muslim. This report does not deal with the parts of Kashmir that are administered by China. We have used the shorthand "J&K" to refer to the Indian parts of Kashmir, "AJK" to refer to Azad Kashmir, and "NA" to refer to the Northern Areas.

Sluggish production of major agricultural crops, a devastating lack of jobs, especially outside the government, and a poor investment climate are among the serious problems shared across the Line of Control. Though some sectors have done well—horticulture and handicrafts in J&K, and construction and the security "industry" on both sides of the line—dependence on government transfers is extraordinarily high. On both sides, the state government is the largest nonagricultural employer.

Jammu and Kashmir

On the Indian side of the line, J&K's sluggish growth and a decade of stagnation in per capita income coexist with a relatively high level of per capita consumption. The percentage of people in poverty is no higher than in the rest of India and may be lower. Literacy is significantly lower than for India as a whole, but spending on education and health is well above the national average.

Infrastructure is a problem area. J&K has tremendous unrealized potential for hydroelectric power, and electrical generators lose nearly half their output to transmission and distribution losses. Rail lines stop at Jammu; road links both within Kashmir and to the rest of India are inadequate and now badly disrupted by the

earthquake. Telecommunications have improved significantly in the past five years, but teledensity is still only half the level of the rest of India. Air travel is especially important given the problems of land transport.

Environmental degradation has taken an alarming toll. Water pollution will have lasting health effects and will undermine both agriculture and efforts to revive tourism. Kashmir's forests, which should be a major resource, are being depleted by illegal logging.

Looking sector by sector at the economy, major agricultural crops have stagnated in the past decade, but horticulture has done well, in some ways benefiting from changes in marketing patterns induced by the insurgency. Tourism all but disappeared during the worst years of the insurgency but has recovered to about one-third of its pre-1989 level. Economic and industrial revival programs from both the state and the national governments have moved slowly and have had limited effects. Until the security situation improves, major changes in the investment picture are unlikely.

These problems affect all parts of J&K. Jammu is less affected than the Valley of Kashmir by insecurity; hence, it has done slightly better in attracting investment. Jammu also supports a significant population of Hindus driven out of the Valley of Kashmir by the insurgency. Everyone agrees that the Pandits, as they are called, must be reintegrated, but no preparations for that kind of integration have been made. Ladakh has two additional problems: physically, it is most easily accessible through Kashmir and consequently affected by the insecurity there; and its harsh but fragile environment is under tremendous pressure.

Azad Kashmir and the Northern Areas

The two areas administered by Pakistan are quite distinct, physically and in every other way. Azad Kashmir has per capita income substantially below that of the rest of Pakistan. Literacy, however, is substantially above the rest of Pakistan, and the situation of women compares favorably with the national scene. Its economy is driven chiefly by agriculture but also relies heavily on remittances. The southern part of Azad Kashmir sends many young men to the Pakistan army; others go to Europe or the Persian Gulf. Tourism has some potential but is essentially undeveloped. The state government, with national support, is supporting a refugee population of some 54,000, many of whom have come to Azad Kashmir from Indian-administered parts of the state. Individual refugees have little incentive to become self-supporting, because they lose financial benefits if they leave the refugee support system. Azad Kashmir is home to most of those killed or wounded by the earthquake and to many of the homeless. Relief and reconstruction will be its major preoccupation for the next year or so.

The Northern Areas have an income level just over half that of the rest of Pakistan, low health and literacy, and a high incidence of poverty. However, they have made remarkable progress on the social side in the past 20 years, thanks in part to remarkable work by the Aga Khan Rural Support Program. This region is sparsely populated and remote and will always be somewhat of a "niche" pastoral economy,

but it has begun to develop an interesting tourism industry following the opening of the Karakorum Highway.

Recommendations

The recommendations in this report aim at improving the economy and increasing the linkages between the regions of Kashmir and between Kashmir and the surrounding countries. Ultimately, this will require a more vigorous private economy. Private investment in J&K is unlikely to pick up until security conditions have improved, however. In AJK and the Northern Areas, the absence of a settlement and their relative remoteness from Pakistan's economic heartland discourage investment.

Our recommendations are organized into 11 topical clusters. Many can be carried out unilaterally, without coordination between India and Pakistan. These include economic development initiatives, employment programs, much of the needed infrastructure creation, and environmental cleanup. The most powerful of these unilateral measures include:

- *Expanding employment* on both sides, using badly needed public works in such areas as road building and environmental cleanup.
- *Creating in Srinagar the business services needed to expand trade, including a one-stop "dry port"* that provides export documentation, packaging, and customs processing; bonded trucking and rail service; and a container depot featuring containers small enough to fit through the road tunnels leading into and out of J&K. This would be the lead item in an overall program intended to expand trade between Kashmir and both India and Pakistan, as well as with the outside world.
- *Designating Srinagar Airport as an international airport with the full range of services*, so as to permit direct exports, charter flights for tourists, and eventually package tourist deals including destinations on both sides of the Line of Control.
- *Developing refugee resettlement plans* for both the Hindu Pandits driven out of the Valley of Kashmir and the refugees in AJK. Both groups are suffering, and risk becoming obstacles to a settlement unless they are given a stake in peace.
- *Encouraging India to open up J&K to foreign bilateral aid donors.* Current Indian policy limiting the foreign aid presence to multilateral donors cuts off an important avenue of funding for development projects in J&K. Bilateral aid could play an important role in financing many of the initiatives put forth in this report.

The most powerful engines of economic growth and integration require joint action and, in several cases, private support. Some of these are practicable today and could be looked on as early steps in a peace process that is likely to last at least several years. Others should be considered as ingredients in an eventual settlement. The key recommendations in this category are:

- *Integrating earthquake relief and reconstruction activities across the Line of Control, and developing integrated plans for future disasters.*
- *Opening the road between the two sides of Kashmir to trade and truck traffic, which both Indians and Pakistanis are in principle willing to do. The initiation of bus service has whetted people's appetites for more.*
- *Joint initiatives on water management and the environment, under which local authorities in AJK and J&K meet periodically, exchange data on water quality and water flows, and consult with one another on environmental problems they share. Pakistan's and AJK's rivers all flow through J&K first, and water quality as well as water supply are an increasingly urgent issue in the region.*
- *A Joint Kashmir Tourism Development Board, composed primarily of representatives of the tourist-related industries in AJK, the Northern Areas, and J&K, but also including representatives of the AJK and J&K governments and observers from Islamabad and New Delhi. It would facilitate the development of facilities and commercial packages bringing tourists to both sides of Kashmir.*
- *Linking the electricity grids on both sides of Kashmir. Hydroelectric power is one of the most important resources in AJK and an important potential resource in J&K. The two sides' needs are complementary, and a grid connection would sidestep the restrictions on power development in Kashmir under the Indus Waters Treaty. It is not too early to start looking at concrete ways of managing the political risk this would involve.*
- *An ecological science park near the Siachen and Baltoro Glaciers. A proposal for such a park has been under development for some time, and studies by scientists affirm its likely scientific value. It would serve as a powerful symbol of a new India-Pakistan relationship. The current cease-fire along the Line of Control makes it possible to think seriously about such a proposal. It would have to be preceded by an understanding between the Indian and Pakistani armies on demilitarizing the Siachen area.*

The recommendations listed above, as well as the others contained in the main body of this report, would all contribute to our twin goals of economic improvement and peace-building, but they are inherently limited. Our final recommendation is more ambitious and more visionary. It would open up the possibility of a more dynamic and prosperous economy extending not only to Kashmir but throughout the region.

- *Creating a special economic zone in all of Kashmir, with duty-free access to India and Pakistan and including an institutional framework for joint investment. This would build on the trade liberalization agreements reached within the South Asian Association for Regional Cooperation (SAARC). Taking as a point of departure the framework that now exists in both India and Pakistan for export promotion zones, it would provide not only for duty-free exports to India and Pakistan, but also for duty-free imports of inputs, for appropriate tax breaks and especially regulatory simplification for participating enterprises, and for accelerated creation of the necessary infrastructure. It would place considerable*

demands on the governance structure on both sides, to ensure that the tax and import duty treatment did not lead to abuses. The tourism, transportation, electric power, and information technology sectors would be promising areas for investment.

Such an arrangement could be implemented under a variety of political and territorial settlements of Kashmir. It would be a departure from current economic policies in India and Pakistan and from the patterns prevalent in India-Pakistan relations. But both India and Pakistan have taken significant steps in the past 10 years to integrate their economies with the rest of the world and with their neighbors in South Asia. In that sense, a “Kashmir Special Economic Zone” represents a logical extension of the policies both countries have been trying to implement.

All the recommendations for joint action require more India-Pakistan cooperation than is in practice today. The proposal for a special economic zone requires major changes in the domestic economic policies of both countries and, indeed, a new way of looking at economic relationships. Even some of the unilateral recommendations require rethinking the relationship between both parts of Kashmir and the ties between India and Pakistan, as well as the parts of Kashmir they currently hold. This will take time.

This is not a reason to set them aside, however. Rather, it is an argument for creating a more peaceful environment in which they can succeed. As part of that process, we have included a series of recommendations for academic and cultural exchanges. These may not, strictly speaking, be economic proposals, but they would, if implemented, help lay the groundwork for this more ambitious vision of what Indians, Pakistanis, and Kashmiris might accomplish together.