

A Difficult Road to Eurasian Economic Integration

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Abstract

In 2010, almost two decades after the collapse of the Soviet Union, Russia, Kazakhstan and Belarus formally started a process of economic integration by establishing a three-country Customs Union. The article analyses the development of this project since then, highlighting both the achievements made by its participants and problems that they are facing.

In January 2012, the implementation of an ambitious project of economic integration between Russia, Kazakhstan and Belarus moved into its second stage, with the inauguration of the Common Economic Space (CES). During the first stage of this project (2010–2011), these three major post-Soviet countries established a Customs Union (CU). As part of this process of creating a Customs Union, the founding member-states adopted unified rules and procedures regulating their mutual trade, established a single customs tariff (SCT) and a unified customs area. They also founded a CU Commission as a special body with supra-national powers to manage the Customs Union's activities. The CU member-states also agreed to establish unified non-tariff protection measures, as well as anti-dumping legislation and compensatory tariffs, in their trade with other countries. In addition, in July 2011 the CU member-states took a significant step forward in their economic cooperation, by abolishing customs controls on their common borders.

After only two years of the CU's existence, it is too early to expect any major economic benefits to be derived by these countries from their membership. And yet such benefits have already started to accumulate and become increasingly obvious.

Following the lifting of customs barriers on trade between Russia, Kazakhstan and Belarus in 2011, the size of their mutual trade turnover jumped by over 35 per cent, exceeding the growth rates of their trade with other countries. Also, as a result of easing border procedures, the time needed for transportation of goods across their common borders was reduced substantially. Moreover, with the total package of CU regulations coming into force, free transit of goods across territories of the CU member-states is now allowed.

This does not mean, of course, that conducting trade between Russia, Kazakhstan and Belarus has become problem-free. In fact there still remain a number of problems and contradictions which continue to stand in the way of the development of mutually beneficial business relations between them. Some of these problems are a result of technical mistakes and discrepancies, and are thus relatively easy to deal with. Others, however, are more serious and are of a more fundamental

nature, reflecting differences in the national and business interests of CU's member-states, which have accumulated over two decades of their sovereign existence since the collapse of the Soviet Union.

The newly established CU Commission was entrusted with resolving these problems by streamlining disputed rules and procedures. It was also authorized to single out the most "sensitive" commodities for each of the CU members and, in order to preserve economic stability, set custom tariffs for such commodities that would be different from the SCT, but valid for a certain transitional period only.

Yet, for the most part CU trade policy was aimed at protecting interests of national production in the member-states and at promoting cooperation between them, not by making temporary exclusions from the SCT or adopting protection measures, but by carrying out a coordinated policy of creating the most favorable conditions for business activities across the unified customs area.

These purposes were served, firstly, by the abolishment of customs controls on the CU internal borders. As a result, numerous barriers impeding normal business activities were lifted. Thus, an important step was made in promoting national business, to reduce production costs and overhead expenses and, consequently, to bring down consumer prices.

Secondly, the CU member-states agreed to continue coordinating their policies on those issues where serious differences still existed. The need for such coordination was needed as, for instance, the level of taxation on business activities in Kazakhstan was markedly lower than in the other two CU member-states, while agricultural production in Belarus was heavily subsidized by the government.

Thirdly, additional efforts were taken to resolve differences, which sometimes were very sharp, between the CU member-states in certain areas of their business interaction.

Probably the most serious and painful among them were differences between Russia and Belarus on trade in energy commodities. While Belarus wanted free import of Russian oil and gas at discounted prices or even at Russia's domestic prices, Russia, on the other hand, was pre-

pared to export only a limited amount of energy products to Belarus on such terms and only for Belorussian domestic consumption. The Russians argued that Belarus wanted, in fact, to import cheap Russian oil and gas in excess of domestic consumption and then re-export the excess to other countries at much higher international prices, which, they claimed, would amount to direct subsidizing of the Belorussian economy at Russia's expense.

To resolve these differences Russia and Belarus conducted several rounds of negotiations in 2010 and 2011. The atmosphere at the negotiations, which periodically were bordering on collapse, was very tough. The participants, however, understood quite clearly that if the talks collapsed then the future of the Customs Union was doomed to failure and the continuation of economic integration between Russia and Belarus would be impossible. Against this background, they managed, therefore, to avoid such a negative scenario and finally reached a compromise on the major issues under discussion.

Thus at the end of 2010, Belarus confirmed its intention to continue its participation in the integration project with Russia and Kazakhstan by official ratifying the accession documents to the Common Economic Space. In response, Russia announced the introduction of the so-called integration coefficient to be used for the progressive reduction of Russian gas prices for Belarus.

These steps were followed by the conclusion of an inter-governmental agreement between Russia and Belarus at the beginning of 2012. Under its terms, the price for Russian gas exports to Belarus in 2012 is set at the level of US\$ 165.5 per 1000 cubic meters, or at the closest level to Russian domestic prices. Russia also agreed to Belarus's insistent requests to sell it over 21 million tons of tax-free oil, thus actually providing its neighbor with a subsidy of US\$ 4.3 billion. In response, however, Russia established its full control over the Belarus gas transport company "Beltransgas".

Yet, in spite of these and other difficulties, the CU member-states view the results of the first two years of the Customs Union activities positively and as such have decided to move into the second stage of economic integration, by launching the Common Economic Space from January 2012.

This decision was reflected in the Declaration of Eurasian economic integration, which was signed by the Presidents of Russia, Kazakhstan and Belarus on 18 November 2011. As a result of the formation of the CES, not only will free movement of goods be possible across the territories of Russia, Kazakhstan and Belarus, but also the free movement of services, capital and labor. In order to convert this political statement into an economic reality, the participating countries decided to coordinate their industrial, transport, agricultural and energy

policies, as well as to promote cooperation in production, including the possible formation of joint transnational corporations. They also pledged to continue harmonizing their national legislation in areas specified by the 17 agreements that form the legal basis of the CES.

The new format of economic integration also required further perfection of the management of economic integration. It was therefore decided that the CU Commission was to be replaced from 1 July 2012, by the Eurasian Economic Commission (EEC), which has its headquarters in Moscow. The functions of the EEC were expanded substantially to cover (a) implementation of a coordinated macro-economic policy between CES countries; (b) setting up of unified trade regimes with other countries; (c) regulation of the activities of natural monopolies; and (d) development of a unified policy of supporting industrial and agricultural production.

In order to upgrade the authority of the EEC, it was decided that its structure would be a double-level one. At its upper level would sit three appointed Deputy Prime Ministers from each of the participating countries. All the current activities of EEC, including custom taxation, setting up sanitary, veterinary and migration norms and regulations, as well as observation of distribution of industrial and agricultural subsidies, are carried out at its lower level by a Board of Experts and its Chairman, who will be appointed for a four-year period.

Decisions taken by the EEC are to be obligatory for implementation by all member-states of the Common Economic Space. However, in order to guarantee protection of their national interests, it was decided that if the EEC failed to reach an agreement on a certain issue, the final decision will be taken by the Higher Eurasian Economic Council, which consists of the Presidents of the CES member-states and can only be passed by consensus.

It was also decided that the Eurasian Court, established formally back in 2000 but that has been lying dormant since then, should at last become operational. Its services have actually only been called upon when integration processes within the post-Soviet space started to accelerate, and the need for objective settlement of economic disputes, as well as for uniform application of agreements reached between members of the emerging integration structures, grew.

Consequently, the Eurasian Court, the headquarters of which are in Minsk, began to function on 1 January 2012. According to its status, the Court was entrusted with examining economic disputes between member-states of the Customs Union and the Common Economic Space or between individual companies and business corporations from these countries. The verdicts of the Court in such cases are to be obligatory for all parties to a dispute.

The Declaration of Eurasian economic integration set not only short-term goals aimed at a more efficient functioning of the CU and CES, but also targets for the continuous development of their legal basis and perfection of their management. The most important part of the Declaration was that it announced the intention of the participating countries to complete by 1 January 2015 all preparations necessary for the establishment of the Eurasian Economic Union.

The idea of establishing such a Union was initially launched by Kazakhstan's President, Nursultan Nazarbayev, as far back as March 1994. However, his proposal did not raise any interest among the other post-Soviet states, either then or during the next several years. There was little interest in this proposal because in the initial period of their sovereign existence, the newly independent states from the Soviet Union aspired to maximize their economic independence and were thus conducting centrifugal policies. It was only in the first decade of the new century that due to a number of both domestic and international trends, which had a negative impact on the economic and social development of the majority of post-Soviet states, that these centrifugal tendencies in their policies began to be replaced with centripetal ones. Consequently, these states started to restore and strengthen bi-lateral, as well as multi-lateral, ties with each other, not only in economic, but also in political, relations, as well as on issues of international and regional security.

These changes were reflected in the formation of the Customs Union and then of the Common Economic Space between Russia, Kazakhstan and Belarus. Another manifestation of this strengthening of economic cooperation between post-Soviet countries was given by the establishment of a common free trade zone under the auspices of Commonwealth of Independent States. An agreement to this effect was signed by Russia, Ukraine, Belarus, Kazakhstan, Armenia, Kyrgyzstan, Moldova and Tajikistan in October 2011. In other words, economic cooperation between post-Soviet states has started to gain momentum, although in different forms and in varying combinations of its participants. Within this context, the intention of Russia, Kazakhstan and Belarus to move to the next stage of economic integration and to establish a full-scale economic union by 2015 constitutes an important part of this process.

However, these integration projects face new challenges. The most serious among them may come as a result of some CU and CES member-states joining the World Trade Organization ahead of others. At the end of 2011, after almost two decades of intense negotiations, Russia's request for admittance to the WTO was finally approved at the ministerial conference of this

organization. As a consequence, Russia's partners in the CU and CES, even though not yet themselves members of the WTO, are now expected to meet WTO obligations similar to those undertaken by Russia. Obviously, under such conditions, it was necessary for all the countries involved to find a way out that would help them to avoid conflict between their national economic interests, without sacrificing their obligations either to the WTO or to the CU/CES.

Of course, this development did not come as a total surprise, since at the very beginning of the formation of the Customs Union, its members agreed that both the CU, and then the Common Economic Space, would be established on the basis of WTO norms and regulations. Hence, Russia, Belarus and Kazakhstan have tried to follow these conditions diligently, while building up their common trade policy. They also announced their intention to make their Customs Union a collective member of the WTO (as is the case with the European Union) after all of the member states have joined this organization.

Moreover, the existing preferential trade regime on the territory of all three CU member-states does not, in fact, contradict international practice and WTO principles, such as participation of WTO members in preferential trade agreements (PTAs). The number of such trade agreements grew up from approximately 70 in 1990 to almost 300 in 2010. And on the average every WTO member now participates in 13 PTAs. Also among the participants in PTAs are both developing, as well as industrial nations. Nevertheless, the Customs Union of Russia, Kazakhstan and Belarus will need to somehow adapt its earlier established SCT rates and import substitution programs to these new conditions.

It is safe to predict also that the member-states of the future Eurasian Economic Union will face further and no less difficult challenges, as, for instance, the formation of a coordinated/single monetary policy and the establishment of a single currency. Obviously, success or failure of the Eurasian Economic Union project will depend firstly, and above all, on the state of the domestic economic situation in Russia, Kazakhstan and Belarus. They will need, however, to draw proper conclusions from the experience of the European Union, as it lives through its current serious crisis. It is not by accident, therefore, that future members of the Eurasian Economic Union are already conducting consultations regarding mutual obligations to maintain specified limits of state budget deficits, or the ratio of state debt to GNP, or the maximum size of inflation.

Still, in spite of the already existing and expected problems and challenges, experts from the CU and CES member-countries tend to have reached favorable con-

clusions about the macro-economic effects of the current, as well as, future integration measures.

Indeed, a report by the Centre for Integration Studies of the Eurasian Development Bank that was published at the beginning of 2012, forecasts that the formation of the Common Economic Space between Russia, Kazakhstan and Belarus will have a positive impact on the development of the countries involved, contribute to deep structural changes in their economies and facilitate their mutual trade and GNP growth rates.

According to this report, by the year 2030 the greatest macro-economic effect from integration will have been witnessed in Belarus, with a substantial increase in its machine-building and food-processing sectors predicted. Economic integration with Russia and Belarus will allow Kazakhstan to upgrade the technological level of its industrial output and radically reduce energy and materials consumption per unit of production. The over-reliance on the mining sector and metallurgy in Kazakhstan's economy is projected to gradually decline, while serious changes in its structure will come as a result of higher growth rates in the service sector, machine-building industries, transportation and communications.

Also, the report forecasts that over the period of 2011–2030, the cumulative effect of economic integration within the framework of the Common Economic

Space may reach US\$ 632 (in 2010 prices) for Russia, US\$ 106.6 for Kazakhstan and US\$ 170 for Belarus.

Admittedly, these forecasts may seem to be overly optimistic, and will quite likely undergo certain corrections and changes in the future. What is important, however, is that the report reflects changes in the economic mood within the CU and CES member countries, whereby integration plans and emerging business opportunities linked to them are stimulating growing interest among society, and local business circles in particular.

As a consequence, integration processes in the post-Soviet space are no longer restricted to government or government-sponsored programs, but are characterized by an increased involvement of private business. This is because private businessmen have begun to recognize the benefits created by the emergence of a new common market, by the formation of a unified customs area, by the unification of services rates, by the prospects of a free flow of labor, etc. As a result, private businessmen are starting to put forward their own initiatives provoked by these new developments. This growing interaction between government and private activities will begin to transform economic integration in the post-Soviet space, from a process initiated from "above", largely from the political level, into an integral part of the routine everyday economic life of the countries taking part in it.

About the Author

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ANALYSIS

When the "Near Abroad" Looks at Russia: the Eurasian Union Project as Seen from the Southern Republics

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Abstract

Moscow's role and legitimacy in the post-Soviet space is widely discussed within CIS countries. Beyond the divergences of opinion concerning the merits of the Eurasian Union project, a key element underlying the prevailing skepticism about Russian-led integration in Central Asia and the South Caucasus is the low level of trust in the Kremlin's capabilities and capacity to effectively manage such an integration project.

The view of Russia held by other former Soviet republics is extremely diversified and varies from country to country, but also from group to group within countries: political authorities, economic circles, intellectu-

als with nationalist sensibilities, Russian minorities or minorities supported by Russia. These countries and groups perceive Moscow's role and legitimacy in the post-Soviet space differently. Moreover, the projects of