

## THE EURASIAN ECONOMIC UNION, RUSSIA'S INTEGRATION POLICY AND THE EU CHALLENGE

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### *A new phase of Eurasian integration*

In the wake of globalisation, governments have started to see relative advantage in associating with other countries, and also possible negative consequences in staying outside preferential trade arrangements. Many times a decision to join an economic organisation is made because staying outside will be with time more costly. It can be assumed that countries that rely to a very high extent on special export sectors or export partners are hit relatively harder when they are forced to stay outside a free trade area or a customs union. For the exporter, this is because it might be difficult to find alternative markets to sell to or to restructure the country's export composition. Such countries are also very vulnerable to economic blackmailing because sanctions can be addressed to small but crucial sectors.<sup>1</sup>

Since the collapse of the Soviet Union, Russia has sought to establish economic and political alliances with the newly-independent countries of the former Soviet Union (FSU). The Council for Mutual Economic Assistance (CMEA) (1949-1991) and the Warsaw Pact (1955-1991) have been followed by various attempts at cooperation in the post-Soviet space, all of which have reflected both Russia's ability as well as its wish to regain its position as a regional hegemon. The Commonwealth of

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<sup>1</sup> Georgian wines and mineral waters are a prime example of this. They were banned from the Russian market in 2006 until Russia lifted the embargo in 2013. As Russia was the main export market for Georgian wines and mineral waters, Georgian wine producers were forced to improve quality and find new markets in Europe and Asia. Yigal Schleifer, Georgia: Lifting of Russian Wine Embargo to Have Limited Economic Impact?, eurasianet.org, 14.8.2013, <http://www.eurasianet.org/node/67391>.

Independent States was established immediately after the collapse of the Soviet empire. In the 2000s, the economic integration process between the few most interested countries, Russia, Kazakhstan and Belarus, has been rapid.

The Eurasian Economic Union, EEU, which is the latest phase in the continuum of Russian-led cooperation projects, has been one of the major foreign policy goals of Vladimir Putin. It was built on the already existing Eurasian Customs Union (ECU), as the presidents of Belarus, Kazakhstan and Russia signed the treaty founding the EEU. The signing ceremony was on 29 May 2014, and the organisation started operating in January 2015 with three founding member states. Armenia joined a few months behind and the prospects are that Kirgizstan will follow next.<sup>2</sup>

The founding document established the international legal status, organisational framework, goals and operating mechanisms of the Union. The EEU will base its executive body in Moscow, the high court in Minsk and the top financial regulator in Astana. It seeks to provide closer economic integration between the member states who, signing the treaty, undertook obligations to guarantee the free movement of goods, services, capitals, and labour. The member states will pursue a coordinated policy in key sectors of the economy: energy, industrial production, agriculture, and transport.

However, the treaty stops short of introducing a single currency. It also delays the creation of a common energy market. In fact, based on the first press commentaries in the summer of 2014, Russian experts were cautioning against haste in establishing a single energy market. As a protective measure pursued particularly by Russia, there will be an 11-year-long transition period, during which the member states aim to set up a common oil and gas market. On the other hand, according to Kazakh officials, they see the EEU's immediate benefit as granting landlocked Kazakhstan better access to, and moreover a say in the use of the transport and logistics and other pipeline systems of the Union's member states.

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<sup>2</sup> The Tumultuous Birth of the Eurasian Economic Union, 31.12.2014, <https://www.stratfor.com/analysis/tumultuous-birth-eurasian-economic-union>.

Effective economic integration in the form of a customs union necessitates giving up some sovereignty in favour of a supranational organ that administers common policies. What is received with this decision is a share in the decision-making process of the organisation. Most often the references made about Russia's partners losing their sovereignty in Eurasian integration projects refer to Russia's geopolitical and great power aspirations, which have in fact never been well-hidden (Starr & Cornell, 2014). The discrepancy between what is decided and what is happening in the real political sphere, is a factor that needs to be taken into account when assessing the performance of the Eurasian Union. However, it is important to bear in mind that the Eurasian Union is not all about geopolitics or Russian integration goals. It is an actor in the international arena with a set of rules and established structures and it cannot be analysed without taking into consideration also its working mechanism (Popescu, 2014).

### ***Russian geopolitics, the Eurasian Union and the EU***

The EEU project should be analysed in its geopolitical context. Firstly, it must be noted that Russia's integration policy is connected to its status as a great power. Russia wants to offer the countries of the former Soviet Union (FSU) an alternative integration model.

There has been one small victory and one major blow in the work towards the EEU: in the summer of 2013, Armenia discontinued its negotiations with the EU and announced that it would join the Eurasian Economic Union. In October 2014, it signed the founding treaty, and it became a member at the start of 2015. The government of Ukraine, on the other hand, decided to integrate with the EU instead. On 21 March 2014, it initialled the political sections of its Association Agreement. The DCFTA was signed on 27 June 2014. By taking these steps, Ukraine *de jure* discarded Putin's EEU option.

Russia seeks to attract new members away from the EU orbit with the integration projects. Its integration policy is based on counter-effecting the EU's attraction and that is why it has regarded the Eastern Partnership as a challenge to its interests in the FSU area. The EU's

stated objective in the European Neighbourhood Policy was to share the EU's stability, security and prosperity with neighbouring countries. The policy was designed to prevent the emergence of new dividing lines in Europe by offering neighbouring countries closer political, security, economic and cultural cooperation. However, Russia has regarded the policy as a threat to its security: according to the Russian Foreign Minister Sergey Lavrov, the EU was trying to establish its own sphere of influence through the European Neighbourhood Policy and then later the Eastern Partnership.

The fact that both Russia and the EU wanted the Eastern European countries to join their own integration projects – which are incompatible – has polarised the situation for all countries between Moscow and Brussels. The problems for these countries are caused by the difficult relationship between the two power centres and their unwillingness, or at least incapability, to deal with one another.

The EU's policy towards the Eastern Partnership countries was compatible with their prior commitments. The Association Agreements (AA) were not an attempt to attract the EaP countries from their obligations for instance within the CIS free trade area. On the other hand, the provisions of the Deep and Comprehensive Free Trade Agreements (DCFTAs) the EU offered to the partnership countries are not compatible with membership in the Russian-led Customs Union. And this is where the two integration projects have clashed. (Popescu, 2014)

The EU has neglected to see that Russia analysed the EaP in a very different context than what its purported goal had been. Russia's own EEU project was never just about economics. In fact, it was perhaps not about economics at all. For Russia, and especially President Putin, who has been the primus motor of the project, it was about Eurasia as a geopolitical project (Starr & Cornell, 2014). It needs to be understood that Russia sees the EU's aim to provide these countries possibilities to modernise as a geo-political threat.

### *EEU rules and performance*

However, the EEU is not merely about geopolitics or Russia's great power aspirations. As Dragneva and Wolczuk have pointed out, the latest phase in the form Eurasian customs union has in fact, unlike previous initiatives, had an effect on the member states and their economic actors. They have begun to harmonise legislation and standardise practices and policies (Dragneva & Wolczuk (2012), 5). However, with the crisis in Ukraine and subsequent Russian economic slowdown, the Eurasian Economic Union is facing severe problems. These recent developments notwithstanding, it is nevertheless important to see what kind of an economic and political actor is taking shape in the EU's neighbourhood.

Regional economic organisations ought to bring economic benefit to their members, who will benefit from protectionist policies and be given power to influence the decision-making process and lobby for their national interests. In the EEU's Inter-Parliamentary Assembly, the voting power is based on the size of population. Therefore Russia does possess even an absolute majority of votes, whereas for instance Armenia's has very little voting power. However, at least on paper, the Supreme Eurasian Economic Council, which determines the strategy, direction and prospects of cooperation and makes the final decisions on key goals and targets, works to counterbalance the power asymmetry. It is composed of the heads of state of the member states and its decision making is based on the principle of unanimous voting. Thus, on the highest level of policy-making in the EEU, at least in principle, all members have the same voting power.

More importantly, the unanimity rule gives all members the veto power. This right has been many times referred to by Kazakhstan's president Nursultan Nazarbaev as a sacred component of the EEU decision-making rules. He has threatened that Kazakhstan could even leave the union if its independence is in any way restricted by the organisational rules. Also on other instances, Belarus and Kazakhstan both have already showed their power in the EEU negotiations.

Kazakhstan for instance brought up its scepticism about Armenia joining the organisation, referring to the unresolved Nagorno Karabakh conflict that would be a hazard on the customs union border. Nazarbaev has also given several statements which show that the many differences observed during the years of negotiations, have remained unsettled. Belarus's President Alexander Lukashenko for his part said before the signing of the EEU treaty in May 2014 that he was not fully happy with the deal, but saw it as a compromise. Nazarbayev's statements pointed out exactly the same: the new treaty was based on consensus. Moreover, Nazarbaev and other Kazakh officials have been eager to state that as a result of their demands, all aspects of political integration were removed from the EEU treaty.

Russia's efforts to use the organisation towards (geo)political goals will no doubt be steadfastly objected by Kazakhstan.<sup>3</sup> This could well relieve some pressure that Russia could be thinking of putting on its allies, particularly the smallest one, Armenia, within or through the EEU.

The economic performance of the EEU has so far also left the members looking of more results. The Customs Union, which in effect has meant the imposition of the higher Russian external tariff regime on the other members, is judged to be contrary to the economic interests of both Belarus and Kazakhstan.

Customs unions eliminate barriers to trade between members, which is why they are assumed to provide a considerable increase in intra-bloc trade. And on the other hand, they reduce trade between members and non-members in two ways. This is because the members of a trading bloc substitute their imports from third parties with imports from their own partners. This causes loss of export markets and accompanying revenues to third parties. Furthermore, in order to protect the members' economies, a trading bloc establishes barriers to trade such as customs

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<sup>3</sup> Alex Vatanka, Kazakhstan's Crafty Eurasian Union Strategy, National interest, 20.6.2014, <http://nationalinterest.org/feature/kazakhstans-crafty-urasian-union-strategy-10705?page=2>.

and duties, which might limit or hinder access to their markets, or make the access more costly (Haftel, 2004, 123-125).

However, in the case of the Eurasian Customs Union, its establishment has in fact brought mixed results. This is because Russia has higher levels of protectionism over its domestic market. Customs unions often initially raise the average levels of the members' trade protection vis-à-vis the outside world. In the case of the ECU, the external tariffs were set by Russia's standards which were much higher than the other members'. Kazakhstan, in terms of economic policy the most liberal among the member states, has had to nearly double its external tariffs from 6.5% to 12.1%. This has led to trade diversion, but to Russia's benefit. For instance Kazakhstan and Belarus have not gained significant improvement in their access to Russian markets, and there has been no marked Customs Union-related trade growth as such. For Kazakhstan to start reaping benefits of its membership, the organisation would need to keep to its commitments to foster deeper integration (Carneiro, 2013, 2-3). Recent developments nonetheless indicate that Russia is having trouble playing by the rules of the game.

### ***EEU – which way forward?***

Russia's integration policy involves aligning with someone to defend their interests against the challenge posed by the EU. The principles of Moscow's objections to the EEC/EU have in fact remained constant from the Cold War decades to the present. First of all, Russia is reluctant to deal with a supranational institution. It will counter the EU with a policy of differentiation, opting for bilateral relations instead of negotiating with the organisation as a whole. Secondly, it aspires to limit cooperation to economic affairs only, avoiding sensitive issues such as human rights or other European core values. Thirdly, it wants the EU to accept the *status quo* in the relationship, also an acknowledgement of interests Russia considers privileged. It will also accept a *modus vivendi*, even if this means the continuation of mutual neglect and antagonism. And lastly, it is willing to resort to revisionist methods to achieve its goals (Zagorski, 2013).

This feature will have an effect on all Eurasian integration projects. Russia's decision to use hard economic power in the midst of the escalating Ukrainian crisis is already threatening its commitment to furthering the integration of the EEU. Sanctions against the three states that signed Association Agreements with the EU, Ukraine, Moldova and Georgia, and the ban on food imports from the EU and the US were not sanctioned by the other Customs Union members. Belarus and Kazakhstan chose not to follow these policies. Russia therefore acted unilaterally, and what is more important, it acted in violation of its commitment in the Customs Union.

Russia's independent decisions were against the rules of the organisation and were a serious blow to its credibility in the eyes of outside viewers, and perhaps even more importantly, by Russia's allies and hoped to be allies. The sanctions have created frictions within the organisation leading up to a renewed trade war between Russia and Belarus. The latter has been suspected of exporting western embargoed products to Russia; while both countries have reinstated border controls.

These internal disputes might turn out to bear a devastating impact on the recently established organisation. The poor performance of the Russian economy has been felt in all of the Eurasian union countries, since Russia continues to be their main foreign trade partner. The idea of Eurasian integration and the projects to have come out of it have to large extent been funded by the Russian Federation. The crucial question is how long it will be able to pay the bill of keeping its empire together.

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