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For Russia, Eurasian Union is About Politics, Not Economy

By Alexander Panin

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Russia's Vladimir Putin, right, Kazakhstan's Nursultan Nazarbayev, center, Belarus's Alexander Lukashenko shaking hands in Astana.

With the milestone agreement to create a Eurasian economic union clinched in Kazakhstan on Thursday, Russia put cheap energy resources at the head of its drive to pull former Soviet states away from European integration and into its orbit.

The Eurasian Economic Union agreement, signed by the leaders of Russia, Belarus and Kazakhstan in the Kazakh capital of Astana, will come into force on Jan. 1, 2015. It envisages the gradual integration of the three former Soviet countries' economies, establishing free trade, unbarred financial interaction and unhindered labor migration. The pact combines the previous agreements reached between the three countries under the Customs Union and the Single Economic Space, which were formed in 2010 and 2011 and have been generally considered a success.

At the signing ceremony, President Vladimir Putin said "Today we are creating a powerful center of gravity for economic development, a large regional market that unites more than 170 million people," according to an official transcript.

He also stressed that the union's combined territory is a hydrocarbon treasury, possessing a fifth of all global natural gas resources and 15 percent of all oil reserves.

Russia's gain in entering the Eurasian union is more political than economic — particularly as Russia is still smarting from the recent failure of its attempts to draw Ukraine into the Customs Union. As for Kazakhstan and Belarus, they are pursuing their own economic interests rather than any dream of forming super-state between Europe and Asia, both their leaders and analysts said.

Benefits for Small Ones

A day before flying to Kazakhstan, Belarussian leader Alexander Lukashenko was not overly satisfied with the preliminary terms of the agreement, the signature of which Putin would later call “an epochal event.”

“We offered to conclude a deal with no limitations ... But this is not the agreement we sought and not the one our partners initially spoke of, Russia in particular, ” Lukashenko said at a meeting with ministers in Minsk on Wednesday, the Regnum news agency reported.

He also said that in signing the agreement he is seeking first and foremost benefits for his country, though stressed that Belarus has never been greedy.

One of Belarus's concerns is that the single market being developed does not include energy, meaning that it will have to continue paying duties to Moscow on its exports of oil products based on oil imported from Russia, said Julian Cooper, professor of the Centre for Russian and East European Studies at University of Birmingham.

Belarus buys oil from Russia at Russia's internal price, which is about half the price the world pays on average, and then produces petroleum for export. Until recently, Belarus had to pay customs duties on oil imports for that purpose of up to $4 billion per year, but it has negotiated to subtract $1.5 billion from that sum for next year.

Lukashenko also was promised that export duties will be eliminated when a single market for energy is created, something not planned until 2025.

Kazakhstan, while being historically very supportive of the Eurasian union with Russia and Belarus, had also some concerns of its own.

Speaking at the Higher Eurasian Economic Council last year in Minsk, Kazakh President Nursultan Nazarbaev said Kazakh businesses had been experiencing difficulties exporting their products, especially to Russia.

“Technical barriers on our exports still remain, including sanitation requirements, difficulties with licensing and certification,” he said. news agency Total.kz reported.

These limitations had been particularly hitting Kazakh meat exports, according to Nazarbaev.

“Problems arise because the countries within the union have different technical and sanitation standards for imported products,” said Alexander Knobel, the head of international trade laboratory at the Gaidar Institute.

This, he said, should had been solved within the Customs Union, prior to signing any other agreements.

Hastily Made Agreements

The logical progression of economic integration should have first established the free movement of products within the Customs Union, then go on to the Single Economic Space to ensure an unrestricted provision of services, and only then switched to an economic union where goods and services, finance and labor circulate without restrictions, Knobel said.

Instead, the union is hastily leapfrogging to economic integration while leaving trade issues unsolved, he said.

Initially, the union was slated to have a single market for energy, finance and other areas by 2015. But the new agreement does not say how, for instance, the financial market will be regulated. It just says that it will be a single market starting from 2025. The same applies to oil and gas. Electricity is set to become one market in 2019 while the markets for medical products and pharmaceuticals are scheduled for unification in 2016.

“All of this could have been done within the Customs Union agreement. But at least the sides have now established fixed dates by which they will have to reach further agreements on most important issues,” Knobel said.

According to the Eurasian Commission — the regulatory authority of the Customs Union and the Single Economic Space — trade turnover between the countries of the union in 2013 amounted to $64 billion, down from $67.8 billion a year earlier. By comparison, Russia's trade turnover with Europe last year surpassed $400 billion.

“Trade within the [Eurasian] Union will be less competitive and demanding in terms of the quality of goods and their technological level than trade with economically more advanced partners such as the European Union, U.S. or Japan,” Cooper said, adding that there is a danger that the union may hold back the modernization of all three economies.

At the same time, in the long run the economic integration has high chances of being mutually beneficial for all states, he said: “In time, there should be gains for all three countries as these trade and regulatory freedoms develop, in particular a more favorable business climate may be created with the prospect of increased foreign direct investment.”

The Past And The Future

Russia is likely to draw more partners to the union by transferring resources to them in the form of reduced prices for gas and oil. In this transaction, the incurred loss for Russia is insignificant, while the gain for its partners would be substantial.

An example of this is Armenia, which was set to integrate with Europe but changed its mind after it was offered gas in 2014 at the price paid by Belarus — about $170 to $180 per 1,000 cubic meters, Knobel said.

“For Armenia this is about 1.5 percent of gross domestic product per year, which is very valuable,” he added.

Economic union with Russia is even more profitable for Belarus, Knobel said, as the gains from exploiting oil and gas trade with Russia constitute 10 percent of its economy.

“And with all the discounts underway this figure will grow to 15 percent of GDP, so integration makes a lot of sense,” the analyst said.

Other countries which may join the Eurasian union in the not so distant future include the Central Asian state Kyrgyzstan, whose leader discussed the possibility of joining the pact, Putin said Thursday. Another likely member is Turkey.

“Today, once again, Nazarbaev raised the issue of Turkey as a future member, an interesting prospect and not impossible now that Turkey’s chances of accession to the EU are diminishing,” Cooper said.

But one country that Russia wished to see within the union and that has now been lost is Ukraine.

Russia has already offered Kiev maximum preferences for joining the Customs Union and was ready to yield on absolutely every issue except radically low gas prices. But in 2013, rather than agree to join the Customs Union, Ukraine said it was ready to conclude a landmark trade agreement with the EU.

Last year, Victor Yanukovych, Ukraine's former president, tried to reverse that decision and move closer to Moscow. As a result, he was ousted by street protests. Today, Ukraine's entry into a union with Russia, Belarus and Kazakhstan looks less likely than ever.

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