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Policy brief

The Eurasian
Economic Union:
A Bridge to Nowhere?

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EXECUTIVE SUMMARY

Russia began its campaign against Ukraine out of fear that Kiev was opting out of Russia's plans for Eurasian regional integration in favour of a European future. The fate of Ukraine still hangs in the balance, but meanwhile Russia, along with Belarus, Kazakhstan and Armenia, formed the Eurasian Economic Union (EEU) in January 2015.

From an economic perspective, **the Ukraine crisis has led to reassessment amongst EEU members regarding closer ties with Moscow.** Economic sanctions imposed on Russia, as well as the fall in global oil prices, has led to a ruble crisis that has shown the risks of close economic ties with Russia. All three of Moscow's EEU partners have been impacted by the collapse in the value of Russia's currency. In Armenia, the brutal murder of a family by an off-duty Russian soldier have brought out anti-Russian sentiments, calling into question even Yerevan's once steadfast support of the Eurasian Economic Union. There is also unease across the EEU, in Minsk and Astana in particular, about the political threat posed by the Kremlin, as exemplified perfectly in the latter's action in Ukraine. **These concerns, both economic and political, have led to disunity and reticence in the EEU.**

The Russian government in particular has made clear that it hopes the European Union engages with the the EEU and, in the words of Russian Foreign Minister Lavrov, see the EEU as "a serious element of a bridge between Europe and the Asia-Pacific Region." This brief points out that China, the assumed other side of this "bridge" is unlikely to be a steadfast supporter. Officials in Beijing, while supportive of Russia generally, have their own interests in Central Asia, which wont necessarily be harmed should the EEU fail to develop.

This policy brief concludes that while engagement with the EEU could help develop Russia-West dialogue beyond the current post-Cold War institutions, which have been proved unable to prevent tension, the cost of doing business with the EEU at the current time is simply too high. **Any engagement between the EU and the EEU cannot begin until there has been a satisfactory resolution of the Ukraine crisis,** and even then, Ukraine is only the most pressing obstacle blocking extensive cooperation between the EU and EEU.

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The Eurasian Economic Union: A Bridge to Nowhere?

The establishment of the Eurasian Economic Union (EEU) in January 2015 has been described by Russian state news agency Sputnik as “the birth of a new giant”.¹ The integration of the post-Soviet space has long been a core ambition of Russian president Vladimir Putin, and the foundation of the EEU was supposed to represent the culmination of his efforts to bring Russia’s neighbourhood together under Moscow’s leadership. The launch of the Union has however been overshadowed by Russia’s aggression towards Ukraine, which itself was a result of Moscow’s frantic attempts to keep Ukraine within its sphere of influence.

As a result, media attention has been sparse, and commentaries mostly negative. Yet, a January 2015 paper on relations with Russia issued by the European External Action Service as ‘food for thought’ to EU foreign ministers,² and some influential think tanks from Europe have called for varying degrees of engagement on the part of the EU towards the EEU.³ This policy brief presents the problems facing the Eurasian Economic Union, and argues that the European Union engagement should remain off the table until there has been a satisfactory resolution of the Ukraine crisis.

The view from the members

For Russia, Eurasian integration is more about politics than economics. While access to the Belarusian and Kazakh markets, the potential for EU-area import substitution and enhanced opportunities for businesses on the borders are not insignificant for Russia, the overall economic benefits are far from certain for the Kremlin.⁴

Russia has long sought to secure its interests in the post-Soviet space, and with the EU and China both offering alternatives to closer ties with Russia, the EEU acts as a way of institutionalising Russia’s control over the region. In 2011 Putin wrote that the EEU would be “a powerful supranational association capable of becoming one of the poles in the modern world and serving as an efficient bridge between Europe and the dynamic Asia-Pacific

¹ Eurasian Union: the birth of a new giant, *Sputnik News*, 2nd January 2015, <http://uk.sputniknews.com/world/20150102/1013336624.html>, accessed 29th January 2015

² Issues Paper on relations with Russia, EU Foreign Affairs Council, 19th January 2015

³ Mark Leonard and Ivan Krastev, The New European Disorder, *European Council on Foreign Relations*, November 2014, http://www.ecfr.eu/page/-/ECFR117_TheNewEuropeanDisorder_ESSAY.pdf, accessed 16th February 2015

⁴ Sean Roberts *et al*, The Eurasian Economic Union: Breaking the pattern of post-Soviet integration?, *Finnish Institute of International Affairs*, 11th September 2014, http://www.fii.fi/en/publication/439/the_eurasian_economic_union, accessed 12 February 2015

region.”⁵ In reality, far from being ‘epoch-making’, the EEU is rife with internal divisions that will likely render it ineffective and unattractive to the wider world.

Belarus

For Belarus, a long and steadfast supporter of Russia, the EEU has already lost its shine. Economically speaking, Russia is Belarus’ most important partner. In 2013 Belarussian exports to Russia amounted to US\$16.7bn (45% of total exports) while imports from Russia totalled US\$21.4bn (50% of total imports).⁶ With a GDP of US\$71.7bn, this cannot be understated. When it comes to wider Belarus-EEU trade the benefits of integration are less clear. Kazakhstan is Belarus’ next biggest EEU partner, but exports only accounted for US\$859.3m in 2013, and a paltry US\$57m in imports. The absence of Ukraine from the ranks of the EEU is a big loss for officials in Minsk, as their embattled neighbour accounts for a combined US\$6.3bn trade in goods (approximately 8% of total Belarusian trade).

The Russian ruble crisis, and the seemingly long-term negative projections for the Russian economy, further diminishes the economic advantages of the EEU. In the wake of retaliatory sanctions on European produce by the Russian government, Belarus benefitted by re-exporting European goods to the Russian Federation. Officials in Moscow reacted angrily, banning the import of meat and dairy products from Belarus in November 2014.⁷ These trade spats saw Belarusian President Lukashenka, a long-time Putin ally, arguing that “egregious cases in which the union member countries take unilateral action bypassing the agreements have been recorded.”⁸

The tensions between Belarus and Russia represent more than just economic anxiety. Belarus has watched with unease as Russia flagrantly disregarded Ukraine’s sovereignty. Moscow’s claim that it is acting in the interest of ethnic Russians in Ukraine’s eastern regions will hardly settle the nerves of officials in Minsk, who are all too aware of Belarus’ 8.3% ethnic Russian population and almost universal use of the Russian language.⁹ Lukashenko

⁵ Russia: Dangers of Isolation, *Financial Times*, 8th January 2015, <http://www.ft.com/cms/s/0/657967da-9725-11e4-845a-00144feabdc0.html>, accessed 14 January 2015

⁶ STAN Bilateral Trade in Goods by Industry and End-use, Organisation for Economic Cooperation and Development (OECD), http://stats.oecd.org/Index.aspx?DataSetCode=BTDIXE_I4, accessed 15 January 2015

⁷ Russian watchdog bans imports of 8 Belarusian meat, dairy suppliers, ITAR TASS, <http://itar-tass.com/en/economy/761463>, accessed 12 January 2015

⁸ EEU common market mechanisms unadjusted yet — Lukashenko, ITAR TASS, <http://itar-tass.com/en/economy/771363>, accessed 12 January 2015

⁹ Перепись населения 2009 года, National Statistical Committee of the Republic of Belarus, <http://belstat.gov.by/en/perepis-naseleniya/perepis-naseleniya-2009-goda>, accessed 8th January 2015

made clear his support for Ukraine when he visited his counterpart in Kiev in December 2014.¹⁰

Ultimately, in the words of Belarusian analyst Ryhor Astapenia “Putin’s Eurasian ambitions brought war to Europe and economic crisis to Belarus and its two major trading partners.”¹¹ Russia and Eurasia are no longer the answer to all of Belarus’ problems.

Kazakhstan

Kazakhstan has long been a proponent of Eurasian integration, with President Nursultan Nazarbayev first proposing it in the wake of the collapse of the Soviet Union. Closer cooperation with the post-Soviet space provides Astana with a stepping stone to global competitiveness,¹² and greater access to markets including a combined Russian-Belarusian state procurement market of US\$198bn.¹³ The failure to secure Ukraine’s membership has, however, reduced the economic rationale for Kazakhstan to fully engage with the EEU. Ukraine is Kazakhstan’s third largest import partner,¹⁴ and Kazakhstan is a large purchaser of Ukraine’s iron, steel and heavy machinery. War in the Donbass threatens both Ukraine’s heavy industry in the region (which accounts for a large proportion of total production) and its coal source, which is of course vital for the production of the goods that Kazakhstan imports.

Combined trade in goods between Russia and Kazakhstan stood at US\$23.5bn in 2013, representing almost 18% of Kazakhstan’s trade. However, trade with China brought in only US\$1bn less in the same year. The Russian ruble crisis has seen the cost of Russian imports crash, leading a Kazakh regional Vice-Governor to call for import bans on Russian goods to protect domestic producers.¹⁵ While these bans and some other protective measures are

¹⁰ Belarus’ Lukashenko to Meet With Ukraine’s Poroshenko This Week, *Moscow Times*, 19th December 2015, <http://www.themoscowtimes.com/news/article/belarus-lukashenko-to-meet-with-ukraine-s-poroshenko-this-week/513688.html>, accessed 8th January 2015

¹¹ Ryhor Astapenia, Belarus and the Eurasian Economic Union: the view from Minsk, *European Council on Foreign Relations*, 7th January 2015, http://www.ecfr.eu/article/commentary_belarus_and_the_eurasian_economic_union_the_view_from_minsk, accessed 7th January 2015

¹² The Eurasian Economic Union: Breaking the pattern of post-Soviet integration?, *Finnish Institute of International Affairs*

¹³ Dosym Satpaev, Kazakhstan and the Eurasian Economic Union: the view from Astana, *European Council on Foreign Relations*, 12th January 2015, http://www.ecfr.eu/article/commentary_kazakhstan_and_the_eurasian_economic_union_view_from_astana395, accessed 12th January 2015

¹⁴ OECD STAN Database, *op. cit.*

¹⁵ Calls to ban Russian imports voiced in Kazakhstan, *TengriNews*, 9th February 2015, http://en.tengrinews.kz/politics_sub/Calls-to-ban-Russian-imports-voiced-in-Kazakhstan-258827/, accessed 9th February 2015

feasible within the EEU's emergency provisions, the fact that these calls are coming only one month after the establishment of the trading bloc demonstrate the fragility of the body.

Kazakhstan, like Belarus, is uneasy about closer political ties with Russia too. Four million ethnic Russians live in Kazakhstan,¹⁶ a sobering fact for those in Astana who have observed the bloodshed in Eastern Ukraine. Kazakh President Nazarbayev, one of the early proponents of Eurasian integration, is reported to have played a significant role in the Ukrainian peace negotiations, going as far as to offer his capital as a venue for proposed 'Normandy format' talks.¹⁷

Armenia

The economic benefits of EEU membership for Armenia are limited by its lack of land or sea borders with any of the other members. Moreover, while for Kazakhstan the EEU provides an impetus towards higher competitiveness, Armenia has been a member of the WTO since February 2003. Richard Giragosian, a Yerevan based analyst, points out that EEU membership may have several negative impacts on the Armenian economy.¹⁸ Firstly, as a more open economy Armenia will have to adopt fresh protectionist policies, which could force up consumer prices. Secondly, Armenia will have to adjust away from its recent history of EU focused trade in order to favour EEU counterparts. The Russian ruble crisis has also had a significant impact on Armenia, with the value of remittances from Russia collapsing in late 2014.

Armenia's parliament voted almost unanimously to ratify the EEU treaty in December 2014. The absence of clear economic benefits demonstrates the primarily political importance of close ties with Russia. In exchange for operating its 102nd military base (with some 3-4,000 troops) in Gyumri, in Armenia's north west, Russia provides security assurances, which given the ongoing tensions with Azerbaijan over the disputed Nagorno-Karabakh region, are powerful motivations in Yerevan. Cracks however have appeared in Russia's influence in Armenia, with a negative impact of Moscow selling weapons to Azerbaijan, and more recently of a massacre in Gyumri by a Russia soldier, leading to an upsurge in anti-Russian

¹⁶ North Kazakhstan isn't the next Crimea — yet, *Al Jazeera*, 19th June 2014, <http://america.aljazeera.com/articles/2014/6/19/north-kazakhstanisntthenextcrimeaayet.html>, accessed 16th February 2015

¹⁷ Nursultan Nazarbayev's Ukraine Diplomacy, *Jamestown*, 14th January 2015, http://www.jamestown.org/programs/edm/single/?tx_ttnews%5Btt_news%5D=43400&tx_ttnews%5BbackPid%5D=27&cHash=c4faff780d7d88097cf40a42b54db8ea#.VMj3JNKsWSr, accessed 16th January 2015

¹⁸ Richard Giragosian, Armenia and the Eurasian Economic Union: the view from Yerevan, *European Council on Foreign Relations*, 8th January 2015, http://www.ecfr.eu/article/commentary_armenia_and_the_eurasian_economic_union_the_view_from_yerevan387, accessed 2nd March 2015

sentiment.¹⁹ This anger at Moscow combined with the economic costs of closer ties with Russia, is demonstrative of the potential for weakening the Russo-Armenian relationship.

Enlargement possibilities

Russia's aggression towards Ukraine has shown the political threat the Kremlin can pose to post-Soviet states, while the ensuing economic crisis facing Moscow demonstrates the unreliability of partnering with an unstable Russia. The EEU will have trouble enough holding together its current members, let alone attracting new ones. Kyrgyzstan is set to join in the coming months, but with a GDP of around US\$7.5bn, which itself is under threat from Russian economic contraction, it hardly adds to the weight of this organisation. Uzbekistan has made it quite clear that it will not be joining, Tajikistan's disputes with Kyrgyzstan make its membership unlikely, and Russia's hopes at attracting other members have been dealt a severe blow by the political and economic crisis resulting from Moscow's aggression towards Ukraine.

Connecting Lisbon to Vladivostok... and Beijing?

Sergei Lavrov, Russia's foreign minister, has tried to portray the EEU as "a serious element of a bridge between Europe and the Asia-Pacific Region", suggesting that the EU should abandon plans for a free trade agreement with the U.S. and offering the EU a "unified economic space from Lisbon to Vladivostok."²⁰ Taking the fact that the U.S. represents 17.2% of extra-EU trade, compared with 9.5% for Russia (figures correct for 2013, do not take into account impact of sanctions), should the EU consider the EEU as a partner and a bridge to Asia?

What does China think?

For China, on the one hand, the Eurasian Economic Union fits into its desire for a multipolar world order. Beijing wants many centres of power spread around the world, and a secure and strong Russia can support this. On the other hand, China has strong interests in Central Asia, and has long coveted closer ties with the regimes in the region, so the extent to which the EEU develops will be of concern to Beijing.

Still, China is simply too important to Russia, Kazakhstan and Kyrgyzstan for its interests to be threatened by the EEU development. The importance of China will have been a factor in the EEU postponing a common energy market until 2025. With Kazakhstan and Kyrgyzstan

¹⁹ In Armenia, Brutal Killing Tests Renewed Loyalty To Moscow, *RFE/RL*, 15th January 2015, <http://www.rferl.org/content/armenia-brutal-murder-case-tests-renewed-loyalty-to-moscow/26795702.html>, accessed 15th January 2015

²⁰ A United Eurasia from Lisbon to Vladivostok, *EUObserver*, 5th December 2014, <https://euobserver.com/opinion/126790>, accessed 26 February 2015

both relying on China as a source of investment, China's interests will be represented inside the group. Russia has been keen to show that China is supportive of the EEU, with its Ambassador in Beijing announcing China's interest in a future Free Trade Agreement with the bloc.²¹ China is yet to confirm this interest, but regardless, it demonstrates that the EEU will need leaders in Beijing to lend the EEU economic and political weight. For its part however, China's interests in a stable and secure Central Asia may well be served by the EEU.²²

China then, is likely to support the EEU, but not in a significant way, electing to wait and see how effective the organisation is before investing extensive political and economic capital in its success. On the other hand, while China may not be uncomfortable with a successful EEU, it most likely won't be concerned with a failing one either. The much touted "New Silk Road strategy" championed by Chinese President Xi Jinping, will be there to ensure China's interest in Eurasia.²³ The strategy, which largely leaves out Russia, will bring billions of dollars to infrastructure projects in the region.

How should Europe respond?

Mark Leonard and Ivan Krastev, in a paper for the European Council on Foreign Relations, argue that the Eurasian Union could be "the best hope for the EU to establish working relations with Russia."²⁴ This sentiment is echoed in a widely read paper from the European External Action Service, in which possible engagement with the EEU is suggested as a bargaining chip with Russia.

Whether or not the European Union should view the EEU as a bridge to Eurasia depends largely on the answer to two questions; how sturdy is the construction, and what's the toll? On the first question, this paper has shown the growing divisions between an economically unstable Russia and EEU neighbours who are increasingly sceptical of Moscow's intentions, resulting in an ineffective and weak organisation.

Secondly, and perhaps most importantly, the foreign policy toll for engaging with the EEU is, at today's price, too high. EU engagement would lend the organisation strength it desperately needs. It would both reward Russia and give it a more salient argument as to why other states should join in the future. In light of Russia's aggression towards Ukraine, the

²¹ China and Russia-led Eurasian Economic Union may set up free trade zone, *RT*, 9th February 2015, <http://rt.com/business/230567-china-urasian-economic-union/>, accessed 9th February 2015

²² Vaughan Winterbottom, China and the Eurasian Union: an ambivalent relationship, *GIS*, 17th July 2014, <http://geopolitical-info.com/en/article/1405572855398738000>, accessed 17th July 2014

²³ Min Ye, China's Silk Road Strategy, *Foreign Policy*, 10th November 2014, <http://foreignpolicy.com/2014/11/10/chinas-silk-road-strategy/>, accessed 10th January 2015

²⁴ Mark Leonard and Ivan Krastev, *The New European Disorder*, *European Council on Foreign Relations*, *op. cit.*

EU cannot add legitimacy to Russia's attempts to re-gain control over the post-Soviet space. Initial engagement with the EEU should not be on the agenda of policy-makers in Europe until there has been a satisfactory resolution of the Ukraine crisis. Furthermore, as argued by Rilka Dragneva and Kataryna Wolczuk, "any agreement with the EEU is likely to be, in practice, an agreement with Russia as the latter has monopolised the external agenda of the Eurasian regime."²⁵

It would be unwise for the EU to permanently rule out engagement with the Eurasian Economic Union, as Brussels and the West has had it made abundantly clear that the existing post-Cold War institutional architecture in Europe isn't fit for purpose. Any new options through which the West can engage Russia on an equal footing should be left on the table. However, without a satisfactory resolution of the Ukraine crisis, in which Ukraine's sovereignty is respected and Russian troops have retreated behind Russian borders, even discussions about the terms of future engagement are premature. If this resolution is achieved, and that is an enormous if, then initial engagement with the EEU can proceed. However, the EU must be fully mindful that with concerns regarding energy supply, human rights and a host of frozen conflicts, Ukraine is only the most pressing obstacle to EU-EEU engagement. Only under these circumstances would the political cost of doing business with the EEU be low enough to warrant Brussels' full engagement. In the meantime, the European Union must watch the development of the EEU very closely, to fully ascertain the costs and benefits of engagement.

EU member states should also fully support the initiative of the Latvian Presidency of the EU council to strengthen the EU-Central Asia Strategy. Furthermore, EU policies in the South Caucuses have been found to be inadequate, and significant steps should be taken to improve EU strategy and bilateral relations in the region.²⁶ Eastern Europe and the South Caucuses have already shown their potential to cause problems for Europe, and Central Asia, bordered by major powers and home to large reserves of natural resources, will likely prove its own ability to threaten global security in the coming decades. The EU therefore needs a coherent and effective engagement strategy towards the whole Eurasian region; however a possible future relationship with the EEU should be a small element of it, not a central focus.

²⁵ Rilka Dragneva and Kataryna Wolczuk, The EU and EEU: geopolitical problems cannot be addressed by technocratic measures, *European Leadership Network*, 3rd March 2015, http://www.europeanleadershipnetwork.org/the-eu-and-eeu-geopolitical-problems-cannot-be-addressed-by-technocratic-measures_2490.html, accessed 3rd March 2015

²⁶ Thomas Frear, Abkhazia and the west: Rehabilitating engagement without recognition, *European Leadership Network*, 2nd February 2015, http://www.europeanleadershipnetwork.org/abkhazia-and-the-west-rehabilitating-engagement-without-recognition_2370.html, accessed 2nd February 2015

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