

REGIONAL ECONOMIES

THE COMMON ECONOMIC SPACE OF RUSSIA, BELARUS, AND KAZAKHSTAN: PRESENT AND FUTURE

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Introduction

On 1 January, 2012, the official opening of the Common Economic Space (CES) of Belarus, Kazakhstan, and Russia, which moved customs control to the outer border of the Customs Union (CU) in July 2011, launched a qualitatively new stage in integration development in the post-Soviet expanse. The objective conditions for consolidating economic cooper-

ation among the three countries have long emerged, the technical work, in the best interests of all the partners concerned, has been carried out, and the top leaders are showing sufficient political will. So there is every reason to believe that the driving force behind post-Soviet integration in the CU-CES format has sprung into action.

Flat duty and tax rates on imported goods, sanitary and veterinary control, and technical regulation principles have been in effect for Russia, Belarus, and Kazakhstan alike since the middle of 2011. On 1 January, 2012, a basic set of documents on the CES consisting of 17 agreements came into force that address the rights of migrant workers and the members of their families, standard principles of currency policy, access to railroad transport services, standard regulations for the support of agricultural goods producers, and conditions for ensuring free movement of capital. All of this will help to form a common market with more than 170 million consumers and a total gross product of more than \$1,385 billion.

Systemic organization of the flows of such large-scale economic resources is already generating real benefits; despite the list of goods to which export limits still apply, goods turnover among the participants of the Customs Union has almost doubled. According to experts, by 2015 integration will afford the participants in the Customs Union an additional 15% increase in GDP amounting to approximately \$400 billion.

However, in addition to the surface indices, it is expedient to look deeper and appreciate the other innovation benefits owing to the free movement of goods within the framework of mutual trade among Russia, Belarus, and Kazakhstan, the decrease in financial load on commercial enterprises, the removal of administration barriers, the standardization of customs regulations, and the positive effect of the post-Soviet countries'

economic convergence with the humanitarian sphere.

At present, economic development in the three countries is undergoing a qualitative leap, which is raising the investment appeal of the Customs Union and, since 2012, of the CES as well.

However, according to competent assessments, it will take about 5 years (from 2011 to 2015) for the CES to operate as a full-fledged multilateral union capable of ensuring free movement of goods, services, capital, and labor. What is more, at least 55 international documents and other acts must be adopted for this integration union to function as planned.¹

In these five years, the governments involved will have to carry out more than 70 mandatory measures envisaged by the CES agreements in keeping with the specific deadlines set forth in them. It is worth noting that Russian Government Chairman Vladimir Putin designated 2015 as the date for launching the Eurasian Union.²

In other words, the current tasks involved in making the CES a viable project should be carried out as strategic landmarks are reached for creating a wider and more diverse integration union.

¹ See: "Gensek EvrAzES: EEP polnotsenno zarabotat cherez 5 let," available at [<http://www.regnum.ru/news/1452817.html>], 5 October, 2011.

² See: Premier RF: Evraziiskiy soiuz mozhet zarabotat k 2015 godu," available at [<http://www.regnum.ru/news/1457665.html>], 19 January, 2011.

Profitability of the CU-CES for Russia

No one knows for sure just how profitable the CU-CES will be for Russia as the leading economic entity of integration activity. Customs revenue into the Russian budget was expected to amount to 5.4 trillion rubles by the end of 2011, which testifies to a steady rise in income and shows that Russia's state budget interests are being fully observed within the Customs Union and starting investments have proven their commercial viability.

However, uniting the goods, labor, and capital markets will not enforce Russia's advantages automatically. As the legal foundation for integration takes shape, it will be expedient for Russia to intensify cooperation with its partners in those branches that enhance the common export potential of

the CU while also being strategic for the export potential of Belarus, Kazakhstan, and Kyrgyzstan, which joined the union in October 2011.

The strategic branches for Belarus in large-scale international trade are as follows: mineral fertilizers, lumber, finished meat products, instruments, and ground vehicles.

There are favorable competitive conditions for Kazakhstan to expand the export production of grains and products of the flour-and-cereals industry, mineral fuel, oil and petroleum products, non-organic chemical products, and ferrous and non-ferrous metals.

As for trade with the CIS countries, the most important sectors of the economy for Belarus are the meat-and-milk and food industries (particular confectionary), the energy industry (mineral fuel, oil and petroleum products), the chemical industry (mineral fertilizers, plastics, and chemical fibers), and the textile industry, while for Kazakhstan, they are the manufacture of grains and products of the flour-and-cereals industry, the production of alcoholic and non-alcoholic beverages, mineral fuel, oil and petroleum products, and ferrous and non-ferrous metals.

As world experience shows, the commercial viability of integration products depends not only on direct acquisitions, but also on the opportunities for rational organization of multilateral cooperation and ensuring sustainable leadership.

Judging from the objective characteristics of the current economic situation, Russia has favorable opportunities for assuming leadership over Kazakhstan, Belarus, and Kyrgyzstan, which has also

Table 1

**Share of Main Partners in the Export and Import of the CU,
EurAsEC, and CES Member States (%)**

	Perceptible Share (5-12)	Noteworthy Share (12-25)	Significant Share (25-33)	Predominating Share (more than 33)	Share of other Partners
Belarus	Ukraine, Latvia, Switzerland, Russia, France	The Netherlands	RUSSIA (32)		35
Kazakhstan	Switzerland, RUSSIA (8), France	PRC, Italy			48
Kyrgyzstan	Kazakhstan, Uzbekistan, France, RUSSIA (11)		PRC		33
Russia	PRC, Turkey, Belarus, FRG, Italy, The Netherlands				57
Tajikistan	Iran, Uzbekistan, RUSSIA (10), Turkey			PRC	23
Uzbekistan	—	—	—	—	—

joined the project. Russia continues to hold a strong position not only thanks to its close cooperation with partners in the heat and energy complex, but also to the level of cooperation in transport communications, technical regulations, innovation projects, and other practical areas. In so doing, bilateral goods turnover with Russia remains the main backbone of foreign trade both with its partners in the CU-CES and with all the countries in the post-Soviet expanse (see Tables 1 and 2).³

Table 2

**Share of Main Partners in the Import of CU, EurAsEC,
and CES Member States (%)**

	Perceptible Share (5-12)	Noteworthy Share (12-25)	Significant Share (25-33)	Predominating Share (more than 33)	Share of other Partners
Belarus	Ukraine, FRG			RUSSIA (59)	28
Kazakhstan	Italy, FRG, Ukraine	PRC	RUSSIA (31)		34
Kyrgyzstan	Uzbekistan, Kazakhstan	PRC 21%		RUSSIA (36)	28
Russia	Italy, France, Ukraine, U.S.	FRG, PRC			53
Tajikistan	Uzbekistan, PRC, Kazakhstan		RUSSIA (33)		43
Uzbekistan	—	—	—	—	—

However, to ensure the efficiency of Russia's integration ties with its CU-CES partners on a long-term basis, additional efforts must be exerted to develop economic cooperation among Belarus, Kazakhstan, and Kyrgyzstan. These countries must also increase their contribution to supporting the regional position of the CU-CES and modernizing their own production potential; Russian business is called upon to play an important role in resolving these matters.

Tasks and Opportunities for Russian Business in the Integration Vector

Investment expansion of Russian business in the CU/CES countries is the driving force behind forming a common market and promoting government decisions. The removal of customs barriers is

³ Tables 1 and 2 were compiled on the basis of *EvrAziiskoe ekonomicheskoe soobshchestvo 2000-2010*, Interstate Statistic Board of the CIS, Moscow, 2011; *Statistika stran EvrAzES*, Statistics Collection, Moscow, 2011.

opening up additional opportunities: legal procedures for registering documents will take less time and become easier, while transport costs will be significantly reduced. However, this is still wishful thinking, while reality leaves much to be desired.

- First, the customs legislation of the CU contains provisions that limit the freedom of movement of some goods for which either flat import duty rates have not yet been established, or on which export duties are levied in one of the participating states, or regarding which anti-dumping, special duties, and other protective measures have been instituted.
- Second, the so-called residence principle interferes with free movement of goods, in correspondence with which a company of a CU member state may only carry out customs registration of goods in the country where it is registered.

The corresponding services of the three states may interpret the CU Customs Code regulations differently, which could also be detrimental to business. However, it should be kept in mind that customs legislation is only one of the many legal regulators in the economic sphere. There is also civil and currency legislation, as well as many other elements of law-enforcement practice that have still not been incorporated into economic integration. Successful functioning of the CU requires making businessmen more aware of the cooperation opportunities in those vectors that require coordinating joint efforts.

Moreover, discrepancies have not been overcome in defining the mechanisms for ensuring public procurement, carrying out price formation, combating pirated goods, setting rail fees and amounts of state agricultural support, regulating inbound transportation means, and dealing with other aspects of economic activity.

In addition to the above, there are many other, more complex, problems that have still not been resolved.

The most interesting vectors for large Russian businesses are the production and transportation of hydrocarbons, the energy industry, telecommunications, machine-building, transportation, the banking sector, and agriculture. A promising vector of integration cooperation could be joint projects in metallurgy, specialized branches of the heat and energy complex and military-production complex, airplane construction, ship-building, atomic machine-building, and the manufacture of machine-building commodities and chemical products, as well as intensifying cooperation in the development of high technology.

Medium and small businesses are interested in cooperating in information technology, the banking sphere, insurance activity, and trade.

It stands to reason that Belarus and Kazakhstan have their own business practices, national legislation, and practical application traditions.

The economy of Belarus is currently in need of radical management reforms. The systemic crisis, two devaluations of the national currency, and hyperinflation, as well as belated renunciation of emission support of the real sector and the chronic deficit of the current external balance are creating very poor premises for the country's prosperity in 2012; rigorous structural reforms and restructuring of the economy are due.

Although, on the whole, Russian business has great prospects for advancement on the Belarusian market, it is coming across quite a few non-economic obstacles on its way. These are primarily the political ambitions of the national elite, which are often not underpinned by either economic and organizational, or any other fundamentals. A negative role is also played by the striving of the Belarusian authorities to make use of all kinds of external assistance, while ignoring real economic grounds for cooperation. Many Belarusian companies prefer to do business within the country and make payments and pay taxes through their branches abroad. Many programmers, builders, transportation engi-

neers, as well as companies that render educational, consultation, and translation services do their business offshore.

As for Kazakhstan, more than 70% of the country's oil and gas resources are controlled by Western companies. The real scope of the Russian presence in this leading branch of Kazakhstan is very modest, which cannot be said of China. Kazakhstan prefers to orient itself more toward cooperation with Western and Asian corporations that have the latest and effective technology for the high refining of raw hydrocarbons, than with Russian oil and gas companies, which have been concentrating on "easy projects" that produce rapid profit with minimum investments, whereby long-term investments in geological exploration and exploitation of highly complex fields are shrinking. In other words, Russia needs to put more emphasis on projects designed for the high refining of oil and gas that produce a wide range of high added value products.

The participation of Russian companies in creating a Western Europe-Western China transport corridor is extremely promising in the transport sphere. This involves creating a modern road infrastructure, logistic centers, and networks of comfortable rest places, organizing efficient trade and cargo storage, staffing thousands of jobs, and enhancing the welfare of the people who live along these major routes.

At present, Belarusian and Kazakhstan partners are showing an interest in creating joint ventures with Russian business to establish new logistic routes throughout the entire territory of the Customs Union. This is largely due to the perceptible increase in the amount of cargo shipments through Belarus and Kazakhstan after the union began functioning.

The markets of Kyrgyzstan and Tajikistan, to which Russian, Kazakh, and Belarusian companies will be able to gain free access in the future, can hardly be considered promising. Kyrgyzstan's GDP is limited to approximately \$5 billion (which amounts to only 0.004% of the world GDP), while the average annual income per capita is no higher than \$800. More than 52% of Kyrgyz are poor, while 17.8% are extremely poor; according to the World Bank classification, the republic belongs to the low-income group of countries. The economy of Kyrgyzstan depends entirely on money that comes in from the outside, mainly in the form of loans from the IMF, WB, and donor countries.

The situation in Tajikistan is no better, which is also one of the poorest agricultural-industrial countries of the world. According to the IMF, today as many as 63% of Tajiks live on less than two dollars a day. Experts describe the Tajik economy as having an extremely high level of import dependence and low level of human potential.

Tajikistan's budget has a large deficit. Remittances from migrant workers, most of whom work in Russia, reach 50% of the country's GDP. As per the World Bank's latest *Migration and Remittances Factbook 2011* report, in 2009, Tajikistan ranked first among the countries in which a significant portion of GDP is comprised of remittance flows from migrant workers. Last year, the amount of officially registered remittances to Tajikistan amounted to \$2.1 billion.⁴

The level of representation, activity, and penetration rate of Russian business into the markets of Tajikistan and Kyrgyzstan is not high; moreover, far from all the declared projects are implemented. Some companies, for example, Russian Aluminum, have entirely curtailed their activity in the mentioned countries; several projects have been at the discussion or development stage for several years now (Inter RAO UES/RusGidro), while others have been frozen and remain pending (the exploration and exploitation of oil and gas fields).

Moreover, Russian business has a non-economic price to pay in the markets of Kyrgyzstan and Tajikistan, which is characteristic of developing countries. These are induced by the irrational behavior of the ruling elites, which can cause the slightest change in the political situation in the region to

⁴ [http://www.ng.ru/economics/2011-11-25/1_soyuz.html].

become a reason for renouncing earlier obligations and for the emergence of significant business risks. Another serious obstacle to business development is corruption (even despite the fact that Russian business structures categorize it as “overhead costs”); the situation is also aggravated by the financial crisis.

The negative factors also include the artificially high expectations of the leaders of Kyrgyzstan and Tajikistan, who think their countries are attractive for investment, which is explained by the absence of pertinent information and the pursuit of strictly egotistical interests. Favoritism in job appointments is leading to officials being afraid of letting the people who make government decisions know the real scoop on the sociopolitical and economic situation in the country. As for independent monitoring, there is none.

It is obvious that as the CU takes shape, conflicts of interest could arise among individual business groups, which will be interpreted by all the interested sides as “interstate contradictions.” Most of the problems that arise are usually related to the subjective approaches of the business elites, which frequently do not have an adequate or objective idea of the real state of affairs.

Coordinated mutual concessions are needed to overcome this situation and achieve a mutually beneficial level of cooperation, and, what is particularly important, the sides must manifest a constructive approach when discussing differences.

Balance in the Geographical Expansion of Integration Relations

Many countries, including in the Far Abroad, are interested in expanding the geographical range of cooperation with the integration structures of the CU-CES. However, it is unlikely that any other countries will become members of the CU-CES any time soon. As for Kyrgyzstan, many representatives of its elite continue to have serious doubts about President Almazbek Atambaev’s decision to join the union.

The most likely candidates from among the CIS countries (in particular Tajikistan and Ukraine) which supported the establishment of a Free Trade Area (FTA) in October 2011 associate their development not with enforcing one strategic vector of cooperation but with acquiring external resources from several alternative sources. So if the attitude of potential participants in the CU-CES is to change, a radical shift will need to be achieved in the moods of the ruling circles, not to mention at least a year of intensive targeted preparations.

The potential of economic cooperation in the event that new members join the CU-CES is largely ensured by the regional relations of Russian partners and it would be premature to carry out an in-depth analysis of this process. However, it should be kept in mind that a common service market will begin functioning at the beginning of 2012. There are plans to offer the resident enterprises of the participating states a national regime for rendering services, standardizing requirements, and ensuring mutual recognition of permits in licensed types of activity. In so doing, the common efforts of Russia, Belarus, and Kazakhstan, as well as Kyrgyzstan (although to a lesser degree), will make it possible to ensure the union’s potential, thus encouraging more participants to join the CU-CES. The most probable time for enlargement appears to be 2013-2014.⁵

⁵ During expert discussions of the prospects for enlarging the CU-CES, it is periodically emphasized that only the EurAsEC participating states will be able to contend for membership in the Customs Troika (which now officially has four members). Admittedly, this approach has not been voiced in official discussions.

Keeping in mind that the integration factor in the post-Soviet expanse relies primarily on Russia's resource potential, the short-term prospects for enlargement of the CU-CES are largely determined not by objective (interests in intensifying the complementarity of the economic systems) but by subjective stimulants (moods among the ruling circles of Russian partners).

The politicians and main influence groups of each country in the post-Soviet expanse have different attitudes toward the idea of joining the CU-CES. For example, Ukrainian politicians are mainly against the country becoming a CU member, drawing attention to the risk of a decrease in national sovereignty and emphasizing participation in the EU market, the volume of which is equal to \$16 trillion (this figure is several times higher than the analogous index for the CU). After vacillating for several months, the Tajik elite also developed a negative attitude toward joining the CU-CES, while the Uzbek leadership headed by President Islam Karimov has been even more unenthusiastic.

However, the real results of the initiatives for holding consultations put forward by countries of the Near and Far Abroad showing an interest in cooperation will most likely not be manifested for another 3-4 years.

On the whole, balanced geographical expansion of the CU-CES is dictated by a political choice in favor of either an intensive (enlargement only by means of the EurAsEC member states) or extensive version of integration, a key element of which will be Ukraine's involvement. But both of these hypothetical scenarios also have certain provisions in common, such as refraining from speeding up talks with potential partner states on entry into the CU-CES, introducing a standardized transport and logistics system throughout the entire customs territory keeping in mind advanced international experience, assisting optimization of the investment climate and conditions for conducting business, and paying additional attention to increasing capabilities not only at the level of big, but also of medium business.

Integration Development in Multivectoral Conditions

Integration relations are being established against the background of the participating states' diversified interests. The most graphic manifestation of multivectoral relations has been the change in architecture of foreign trade cooperation in the post-Soviet expanse (including within the framework of the EurAsEC) and departure from the monocentric system of partnership in export and import.⁶

However, the current situation is not creating conditions for a radical reorientation of relations among the partner countries of the CU, EurAsEC, and CES. It is characteristic that during the world economic crisis, the monetary values of exports and imports of the CU-CES and EurAsEC participating states within the integration format and beyond it only underwent significant changes in some cases (in the Tajik and to some degree Kyrgyz vectors).

⁶ At the current stage, the volume of goods turnover with countries beyond the post-Soviet expanse in the three participants of the CU, EurAsEC, and CES—Kazakhstan, Russia, and Tajikistan—tops the volume of goods turnover with integration partners (approximately 74%, 86%, and 53%, respectively) and only in Belarus and Kyrgyzstan does this goods turnover comprise a relatively lesser share in foreign trade cooperation (approximately 45% and 48%, respectively). The significance of multivectoral international economic cooperation of the CU, EurAsEC, and CES participating states is more clearly manifested when comparing the values of the export-import flows that have developed among them, with other CIS countries, and with the broad international environment.

The development of the main integration formats relies not only on the dimensions of reciprocal trade exchange between the member countries, but on their complementarity. This will make it possible to resolve many integration development issues, including those associated with assisting the national economies of Belarus, Kyrgyzstan, and Tajikistan, which have a chronically negative foreign trade balance (beyond the post-Soviet expanse).

Multivectoral economic cooperation among the CU-CES participating states is not creating real premises in the mid term for a breakdown in the integration cooperation system that exists in the post-Soviet expanse. Despite the fact that it intensifies competition among economic interest groups at the top level in each of the partner countries, something else is slowing down the integration trends; the matter concerns the unstable involvement of Russian partners in widespread international division of labor. Foreign trade cooperation of Belarus, Kazakhstan, Kyrgyzstan, and Tajikistan beyond the post-Soviet expanse is limited and not fully underpinned by strong bilateral ties with large counteragents.

Moreover, contemporary multivectoral relations orient Russian partners toward expedient activation of cooperation with the regional environment, whereby not only in the post-Soviet expanse, but also beyond it (in certain vectors).

On the whole, keeping in the mind the current architecture for attracting the interests of participants in the EurAsEC-CU-CES, there are no prerequisites for the appearance of sufficiently strong centers of alternative cooperation. Raising the significance of the external vector by developing economic cooperation with the immediate regional environment (including China) in the mid term is limited for the Russian partners by the narrow range of commodity exchange and insufficient investments (Iran and Turkey), and also by the Chinese policy of step-by-step advance of its interests. However, at present, the level of China's economic presence, even in the economies of Tajikistan and Kyrgyzstan which are more open to it, is not enough to achieve decisive influence in the mid term.

It should be emphasized that the objective economic challenges of multivectoral relations, which reflect its limited orderliness, fragmentariness, and lack of significant contribution to the development of economic cooperation between the CU-CES countries and immediate regional environment, cannot be overcome in the near future. Nevertheless, potential risks are accumulating precisely in this area (particularly in the Central Asia zone). Central Asia's economic cooperation with Iran and Turkey is much lower than it is with China, which could lead in the mid term to an imbalance in cooperation relations on the eastern flank of the CU, EurAsEC, and CES.

In Lieu of a Conclusion: Prospects for Making the CU-CES a Viable Project

An evaluation of the prospects for integration cooperation among Russia, Belarus, and Kazakhstan, as well as Kyrgyzstan, within the framework of the CU, EurAsEC, and CES, keeping in mind foreign experience and possible new members, is extremely interesting when viewed in the context of the tactical and strategic tasks of Russian policy. If it does not integrate with its close neighbors, the common market with which would be as large as the EU's, the Russian economy could find itself bowing further to the raw material demands of the major centers of international influence. Moreover, the integration project should ensure Russia leadership among states whose economic systems can only function with extensive external support. Another challenge for the Russian side is the multivectoral nature of its partners' economic interests, which is having an influence on the resolution of specific issues of multilateral cooperation.

The official assessments which presume that integration will provide the participants in the CU-CES with an additional 15% increase in GDP by 2015 are fully justified. The objective characteristics of the international economic cooperation system of the CU, EurAsEC, and CES participating states make it possible to anticipate significant profit; the Russian nucleus of the latter will ensure stable functioning of the main systemic relations in the mid term. Nevertheless, achieving the designated indices of integration development presumes several specific and targeted steps to ensure stable progressive momentum of integration cooperation.

The matter concerns a balanced attitude toward the initiatives to increase membership in the CU, EurAsEC, and CES aroused by the political context, which is related to the contradictions in the leading circles of the potential candidate countries. In this respect, it is very important for the CU-CES to actively position itself as a participant in widespread international economic cooperation.

Efforts to create a standardized legal field of economic activity within the CU-CES must be intensified, in which unification of currency, financial, and civil regulations will be efficiently introduced (along with the standardization of customs legislation).

For the moment though, the legislative regulatory base of the integration processes lags significantly behind the administrative decisions to simplify customs procedures on the external borders, while instituting supranational structures will not fully resolve the practical tasks of optimizing business activity conditions (primarily Russian).

The system of multivectoral economic cooperation among the CU, EurAsEC, and CES participating countries must be improved with respect to integration development. Multivectoral relations should play a significant role in the economic respect, particularly as a mechanism for involving non-raw material companies of developed industrial countries in modernization of the industrial sector and stepping up Central Asia's economic cooperation with Iran and Turkey, which so far lags perceptibly behind its cooperation with China. It should be noted that the main payoffs of multivectoral relations are primarily manifested in political governance and the differing interests of the elites participating in the distribution of government income.

The favorable prospects for and significant economic benefit to be gained from integration cooperation within the CU, EurAsEC, and CES for Russia, Belarus, and Kazakhstan, as well as for new member Kyrgyzstan, are generated by the objective characteristics of multivectoral interaction. However, implementing a comprehensive integration project in the post-Soviet expanse, just like movement along the Eurasian Union trajectory, depends to a decisive extent on political coordination of the efforts of Russia and its partners, as well as on strengthening the institutional component of supranational regulation of the integration trends.