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The Eurasian Economic Union

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Breaking the pattern of post-Soviet integration?

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Sean Roberts, Anaïs Marin, Arkady Moshes, Katri Pynnöniemi
The Finnish Institute of International Affairs

ULKOPOLIITTINEN INSTITUUTTI
UTRIKESPOLITISKA INSTITUTET
THE FINNISH INSTITUTE OF INTERNATIONAL AFFAIRS

Sean Roberts
Senior Research Fellow
Anaïs Marin
External Contributor, Researcher until December 2013
Arkady Moshes
Programme Director
Katri Pynnöniemi
Senior Research Fellow
The Finnish Institute of International Affairs

The Finnish Institute of International Affairs
Kruunuvuorenkatu 4
FI-00160 Helsinki
tel. +358 9 432 7000
fax. +358 9 432 7799
www.fiia.fi

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EXECUTIVE SUMMARY

The Eurasian Economic Union between Belarus, Kazakhstan and Russia consolidates a market of 170 million people with a combined GDP of almost 3 trillion US dollars. On paper, this union has the potential to transform economic relations in the region and to offer an alternative to the EU in the post-Soviet space.

The Union, which comes into effect from January 2015, marks the latest achievement in the current 'intensive phase' of integration, which has seen the creation of a Eurasian Customs Union (2010), a Single Economic Space (2012) and a Eurasian Economic Commission (2012), all intended to facilitate the four economic freedoms – the free movement of goods, people, services and capital. Expanding the Union is also seen as a priority, with Armenia set to join the Customs Union and Kyrgyzstan already at an advanced stage of negotiation.

However, despite early successes, further deepening and widening of the Union are fraught with difficulties and the pace of integration will inevitably slow, as member states come to terms with the commitments they have made. Plans to deepen the Union have encountered a number of implementation issues leading to multi-speed integration from the outset. Likewise, plans to expand the Union have revealed a creeping politicisation that threatens to undermine the 'economic only' nature of this integration project.

More importantly, the latest phase of post-Soviet integration shows strong signs that the older problems of weak institutions and large asymmetry between member states are continuing to hinder closer ties. Taken together, and against the backdrop of an increasingly hostile international environment that has accompanied the crisis in Ukraine, the Eurasian Economic Union faces an uphill struggle to maintain momentum and deliver the results member states desire.

The The EU's Eastern Neighbourhood and Russia research programme
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Introduction[1]

On 29 May 2014, the presidents of Belarus, Kazakhstan and Russia signed a treaty creating a Eurasian Economic Union (EaEU) between the three states. This treaty, which comes into force in January 2015, builds on the recently established Eurasian Customs Union (January 2010) and is seen as the next stage of integration following the creation of a Single Economic Space in January 2012. Overall, the EaEU will consolidate a common market of 170 million people with a combined GDP of almost 3 trillion US dollars.[2] As such, the EaEU not only promises to transform economic relations in the post-Soviet space, but sustained development may yet see the EaEU develop into a regional counterweight to the EU.

In fact, a case can be made that the EU represents a potential partner, competitor, but also developmental template for the EaEU. As Vladimir Putin acknowledged in 2011, the European Coal and Steel Community took 40 years to become a fully-fledged union, but the appearance of the Eurasian Customs Union and Single Economic Space has been much more dynamic, owing to the experience drawn from the EU and other regional organisations.[3] This open acknowledgement of 'borrowing', together with the continuing view of the EU as the 'gold standard' for regional integration, explains why recent studies of the Eurasian Customs Union have made either explicit comparisons with the EU or implicit comparisons using functionalist approaches. The success of EU integration probably goes some way towards explaining the teleology in some studies, where the post-Soviet space, much like the European space, is seen as destined for ever-increasing integration.[4]

This FIIA Analysis, in contrast, does not approach the subject of Eurasian economic integration through the prism of integration in Europe or in any other part of the world. Instead, the focus is on the trajectory of the EaEU – whether it looks set to break the pattern of so-called 'ink on paper integration' seen in the post-Soviet space over the past two decades, where early optimism and initial gains have been replaced by a lack of implementation and, ultimately, stagnation.[5] This requires consideration of the nature of the Eurasian economic integration, including efforts to deepen and widen the Union, as well as the factors that facilitate and slow the integration process. The major added value of this analysis is that it draws on primary data from over 35 face-to-face interviews conducted with experts and stakeholders in Belarus, Kazakhstan and Russia, as well as Armenia, which is expected to join the Customs Union in 2014.[6] This not only

1 Although this project was conducted on the initiative of the FIIA, we would like to express our gratitude to the Finnish Ministry for Foreign Affairs for their financial assistance. We would also like to thank the Finnish embassies in Moscow and Astana, the Finnish Liaison Office in Minsk and the Embassies of the Republic of Belarus and the Republic of Kazakhstan in Finland for their help in facilitating the travel required for this project. Special thanks are also reserved for Veera Laine for her invaluable assistance, as well as all the interviewees for their illuminating contributions.

2 GDP (current US$), the World Bank.

3 Putin, 2011.

4 For an example of direct comparison between Eurasian and European integration, see Blockman et al., 2012; for a functionalist analytical approach, see Dragneva & Wolczuk, 2012; and for a discussion of U-shaped integration and growing interconnection in the post-Soviet space, see Libman and Vinokurov, 2012. For analysis of the implications of Eurasian economic integration for the EU, see Shumylo-Tapiola, 2012 and Adomeit, 2012.

5 Vinokurov & Libman, 2012, p. 53.

6 In May 2014, Armenia's president, Serzh Sargsyan, stated that negotiations on Armenia's entry to the Customs Union were in their final stages (Sargsyan 2014), although actual membership is expected towards the end of 2014. Overall, this analysis reflects the balance of opinion expressed by all the interviewees, and where possible, reliability was confirmed by triangulating information with secondary sources. A full list of interviewees in each country is given in Appendix 1.

gives voice to all those involved in the integration process, but allows a comparison of each member state within the overall analysis of the EaEU.

The following material is divided into four parts. Part one outlines the origins and objectives of the EaEU, as well as the motivations for individual member states to pursue integration. Part two considers the initial successes of the recent 'intensive phase' of integration seen since 2010, including the creation of the EaEU institutional framework and the initial impact of the Customs Union on economic development. Part three examines some of the problems with deepening and widening the EaEU, while the final section provides extended conclusions as part of an overall assessment of the integration process so far.

The argument put forward in this report is that the three founding members of the EaEU have already achieved notable success in pushing regionalism by creating the institutions needed to deepen and widen the project and to boost economic development. However, the current intensive phase of integration is unsustainable and so the pace of integration will inevitably slow, as member states come to terms with the commitments they have made. More importantly, the latest phase of post-Soviet integration shows strong signs that the older problems of weak institutions and large asymmetry between member states are continuing to hinder economic union.

Origins and objectives of the Eurasian Economic Union

Although Eurasian economic integration is currently enjoying an intensive phase following the creation of the Customs Union on 1 January 2010, the roots of the EaEU actually lie in a much earlier period. The Commonwealth of Independent States (CIS), founded in December 1991, saw an agreement on creating economic union signed as early as January 1993 as part of an attempt to gradually move towards an EU-style common market.[7] In April 1994, Kazakhstan's president, Nursultan Nazarbaev, called for the creation of a Eurasian Union to lessen the impact of the collapse of the USSR, and in 1995, Belarus, Kazakhstan and Russia signed a treaty on creating a customs union.[8] The formation of the Eurasian Economic Community (EurAsEC) in 2000 gave renewed impetus to the idea of a common market and in 2007 Belarus, Kazakhstan and Russia recommitted to creating a customs union, with other EurAsEC members (Kyrgyzstan and Tajikistan) earmarked to join later.

What this tells us is that, despite the recent scholarly interest and media attention surrounding the appearance of the EaEU, Eurasian economic integration is actually a long-term process, and more importantly, an unfinished process rather than a discrete event. Not only does this fact raise our awareness of the difficulties of breaking with the past and reconnecting the post-Soviet space to the mutual benefit of all states involved, but it also raises a number of immediate questions, such as why Eurasian economic integration has taken so long to achieve and why the period following 2010 has seen so much integration activity.

The answer to the first question lies in the mismatch between committing to the principle of economic integration and putting it into practice. It has been noted, for example, that no more than 10 per cent of the 1,500 or so CIS treaties and agreements made since 1991 have actually been implemented.[9] This is viewed partly as a problem of the consensus decision-making procedures in place, but partly as the result of weak institutions, in particular the absence of supranational organs able to regulate

7 Vinokurov 2007, p. 26.

8 See Libman and Vinokurov 2012, Appendix 2 for a chronology of post-Soviet disintegration and integration, 1991–2010. See Nazarbaev 1994 for an early discussion of 'Eurasian Union'.

9 Kobrinskaya, 2007, pp. 14–15.

implementation.[10] As a result, CIS integration in the 1990s saw the inevitable development of multi-speed and multi-level integration, with states allowed to choose their own 'integration package' to suit their needs, but with a high risk of backsliding.[11] There was also a problem of asymmetry – the fear of Russian hegemony and loss of sovereignty among smaller members – which pushed many to develop multi-vectored foreign policies to balance regional players and avoid Russian economic and political domination.[12] This reluctance to commit to Russian-led integration projects was reciprocated, in the 1990s at least, by Russia's own lack of interest in the CIS.[13]

What we see in the period leading up to 2010 is a change in at least two dynamics. The first is a change in Russia's attitude and circumstances, which in comparison to the 1990s, are now much more amenable to integration. By the mid-2000s, Russia was enjoying a more reliable financial base as well as greater control over economic actors at home. Eurasian integration also received a boost during the Medvedev presidency (2008–2012), not because Medvedev was particularly supportive of regionalism, but because Putin assumed the post of prime minister and thus responsibility for economic matters. Putin, it should be noted, more than anyone else within Russia, has helped push the integration project forward.

The second dynamic is a convergence on a genuine belief that integration is an unavoidable global trend and that, increasingly, no country is able to prosper in isolation. There is an acknowledgement that the region is still coming to terms with the effects of the global financial crisis, and that only a joint effort is capable of overcoming the challenges ahead. In 2011, Belarus was hit particularly hard by a spiralling financial crisis, but neither Kazakhstan nor Russia have avoided the negative consequences of the global economic downturn, and so this international factor is seen as one important explanation for the renewed emphasis on economic integration seen since 2010.[14]

In the period 2008–2014, both these dynamics served to reinvigorate the idea of economic integration with two clear objectives. The first objective is obvious – to use integration to achieve economic development. The second objective is the means to this end – to increase existing levels of regionalism by building an effective administrative-bureaucratic infrastructure able to implement the agreements that form the basis of the EaEU. Regionalism is also aimed at deepening integration through realising the four economic freedoms: the freedom of movement of goods, people, services and capital, but also widening integration to include new members and increase overall market size.

In terms of the aims of the individual member states, both Kazakhstan and Belarus see the advantage of gaining access to the huge Russian market of over 143 million people. They also view Eurasian economic integration as a way to achieve modernisation by gradually improving economic competitiveness while avoiding the 'shock' of immediate exposure to the globalised world. This logic is perhaps clearest for Belarus. Even though Belarus is not a member of the World Trade Organisation (WTO), the Customs Union applies WTO rules (Russia's tariff obligations), forcing domestic producers to adapt, but in the limited format of 3 'friendly' states.

In a similar way, Kazakhstan views economic integration as a way to increase firm competitiveness, but as part of an ongoing attempt to secure WTO membership. Kazakhstan also views the Customs Union as a means to protect domestic producers from the effects of trade with third countries, notably the growing

10 Sakwa & Webber, 1999, p. 396.

11 Vinokurov, 2007, p. 40.

12 Libman & Vinokurov, 2012, p. 192; Minasyan, 2012.

13 Sakwa & Webber, 1999, pp. 402–404.

14 For details on the Belarus financial crisis, see Kłysiński 2011.

negative trade balance with China. This touches on an important theme in Eurasian integration – 'sovereignty' – and the desire among all member states to enhance it by engaging in trade creation and trade diversion.

As detailed in the material that follows, for Russia, the economic benefits of union are less certain, although access to the Belarusian market of approximately 9 million people and the Kazakhstani market of 17 million are by no means insignificant. Moreover, the manipulation of both tariff and non-tariff barriers may enable Russia to implement a programme of import substitution, in particular in the automobile and aircraft manufacturing sectors.[15] There is also the benefit of a common market for private interests, as the EaEU immediately provides opportunities for Russian businesses located along the 6,800-km Russia-Kazakhstan border to move their operations and take advantage of the favourable tax climate in the latter.[16]

Intensive integration 2010–2014

The argument advanced in this report is that the three founding members of the EaEU have already achieved notable success in pushing regionalism by creating the institutional framework needed to deepen and widen the project and boost economic development. The latter is seen as a major objective of the Union and is typically formulated in terms of increasing quantitative indicators such as economic growth, trade volumes between member states, manufacturing output, foreign direct investment (FDI), firm competitiveness and consumer choice, but more qualitative outcomes such as an improved business climate are also important.

However, the task of determining the real economic success of economic integration is more complicated than it first appears. What is clear is that the EaEU remains a work in progress and that the relatively short operational existence of the Eurasian Customs Union and Single Economic Space give only an approximate idea of the potential of the EaEU. There is also the problem of the reliability of official statistics across much of the post-Soviet space, as well as an acknowledgement that the removal of tariff barriers between the three member states has led to an unexpected deficit of reliable information on trade flows. These reasons alone should elicit a degree of caution when drawing conclusions on the economic effectiveness of the Customs Union and future EaEU.

In addition, there is the issue of determining the effects of the Customs Union, 2010-2014, on the economic performance of the three member states against the backdrop of global economic conditions. For example, trade volumes among member states show an overall decrease in 2013 compared to 2012 and 2011 (see Table 1) and although media sources were quick to see this as evidence of Customs Union failure, this drop in trade is largely explained by volatility in global commodity markets.

This becomes clearer when we consider the structure of mutual trade between the three Customs Union member states, where trade in mineral products, which includes oil, is by far the largest sector (33% of the total trade volume) followed by machinery, hardware and vehicles (20.4%), metals and derived products (12.9%) and agricultural produce and foodstuffs (12.8%). In fact, in 2013, the decreasing trade volume in mineral products and in those sectors reliant on hydrocarbons (chemical products and related industries) disguises a year-on-year increase in several manufacturing sectors.

15 The Customs Union includes a mechanism for redistributing customs duties among the budgets of the three member states. Increases in certain tariffs that may benefit only one member state can be compensated for by increasing the percentage of tariffs redistributed to the other members.

16 Kazakhstan's tax rate on commercial profits in 2013 was 28.6%, compared to 50.7% in Russia and 54% in Belarus. See total tax rate (% of commercial profits), the World Bank.

2010	Customs Union and Single Economic Space		of which					
			Belarus		Kazakhstan		Russian Federation	
	million US dollars	% to previous year	million US dollars	% to previous year	million US dollars	% to previous year	million US dollars	% to previous year
2010	47,134.6	129.1	10,418.4	148.2	5,999.2	166.6	30,717.0	118.7
2011	63,100.9	133.9	15,182.9	145.7	7,103.3	118.4	40,814.7	132.9
2012	67,856.4	107.5	17,116.3	112.7	6,228.7	87.7	44,511.4	109.1
2013	64,136.1	94.5	17,698.1	103.4	5,863.6	94.1	40,574.4	91.2
Jan-Jun 2014	27,638.7	88.3*	8,005.7	93.7*	2,508.0	77.8*	17,125.0	87.6*

Table 1. Volume of trade between Customs Union member states, 2010–2014.
Source: Evraziiskaya konomicheskaya Komissiya (a). *Comparison to January–June 2013.

Elsewhere, economic indicators show mixed results. Trade between the Customs Union member states, China and the EU, for example, shows little change in the period 2011–2013 (see Table 2), and GDP annual growth as a base indicator of economic development was actually lower in each member state in 2013 compared to 2010 when internal tariffs were abolished.[17] In contrast, and despite problems in accurately measuring FDI due to offshore transfers, in Belarus, Kazakhstan and Russia FDI in 2013 was slightly up on 2010 levels.[18] In terms of improving the business climate in each of the three member states, the World Bank's authoritative 'ease of doing business index' shows improvements for Belarus (rank 63 in 2013 from 67 in 2010), Kazakhstan (50 in 2013 from 58 in 2010) and Russia (92 in 2013 compared to 122 in 2010), although clearly there is much work to be done here.[19]

As for increasing competitiveness, measures tend to be approximate, although the World Economic Forum's Global Competitiveness Index survey of 144 countries (Belarus not included) shows small gains for Kazakhstan in 2013–2014 (rank 50) and Russia (rank 64) compared to the previous year.[20] One alternative indication of increasing competition is found in the frequency of business complaints in the national media directed at competitors. Complaints ranging from Belarusian agricultural machinery producers, to Russian textile producers to Kazakhstani mineral companies serve to highlight the pressures of increasing competition in the conditions of an enlarged market.[21]

Beyond economic indicators, the goal of furthering regionalism has also been highlighted as important for the development of the EaEU. As mentioned, this includes deepening and broadening the integration project, but also creating the institutions able to oversee the integration process. Overall, the creation of the

17 In 2013, GDP growth in Kazakhstan was 6%, slightly down on 2010 levels (7.3%). However, in Belarus (0.9% in 2013 compared to 7.7% in 2010) and Russia (1.3% in 2013 compared to 4.5% in 2010) there was a sharp decrease. See GDP Growth (annual %), the World Bank.

18 Foreign direct investment, net inflows (BoP, current US$), the World Bank.

19 See Ease of doing business index, The World Bank.

20 Global Competitiveness Index, 2013–2014.

21 The absence of reliable economic indicators makes the national press in each member state an alternative source of information on levels of optimism among business leaders, as well as the tensions created by increasing competition.

	EU*		China	
	million US dollars	% to previous year	million US dollars	% to previous year
2011	468,960.2	130.3	107,849.4	142.9
2012	491,123.9	104.8	114,381.2	106.5
2013	492,088.3	99.9	114,587.8	102.3

Table 2. Customs Union trade with the European Union (EU) and China (total turnover). Source: Evraziiskaya Ekonomicheskaya Komissiya (b). *Including the Republic of Croatia from July 1, 2013.

Customs Union in 2010 and Single Economic Space in 2012 were significant moments in realising the free movement of goods between member states, and road maps for gradually realising the free movement of people, services and capital are already in place. The EaEU also took a big step forwards with the establishment of the permanent 'supranational' body in the form of the Eurasian Economic Commission in February 2012.

The main goals of the Commission are to support the functioning of the Customs Union and to facilitate deeper integration. Despite some opinions to the contrary, the Commission actually enjoys a great deal more independence as an institution than is commonly acknowledged and Russian pressure over decision-making is exaggerated. Not only is unanimity voting in place to protect individual members, but the Commission is staffed with highly qualified 'international' bureaucrats who are not permitted to lobby on behalf of national interests.[22] To date, the Commission has proved its effectiveness in terms of operational interference in a number of areas, including state purchases, customs regulations, permits for trafficking goods and import quotas as well as passing a large volume of legislative-regulative documents.

The Commission has also established a number of consulting committees in areas concerning taxation and financial markets, which are seen as important steps towards greater inclusion of the business community in the decision-making process. These consulting committees are accompanied by a variety of forums which typically include representatives from state and private organisations.[23] The Eurasian Commission's Board for Customs Cooperation, for example, has ongoing dialogue with representatives of the business community in each of the three member states, in areas such as customs legislation.

In terms of structure, the Commission consists of a Commission Council, which is the highest body and includes three deputy prime ministers from each member state, as well as a Commission Board. The Eurasian Commission has 23 departments whose jurisdiction is divided between the ministers of the Board. Both the Commission Council and the Board are subordinate to an Inter-Governmental Council which comprises the heads of national government in each member state. This body, in turn, is subordinate to the Supreme Council, which includes member state presidents. The Eurasian Court, which was originally created in October 2000 under the aegis of EurAsEC, completes the institutional framework of the EaEU.

When it comes to widening the integration project – another major objective of the EaEU – the expected addition of Armenia to the Customs Union in 2014 is seen as a concrete achievement, not least because of the impulse it provides for further expansion. Kyrgyzstan is currently at an advanced stage of negotiation

22 There is some qualified majority voting for low-level decision-making within the Commission.

23 Suggestions from these committees are then passed to the Commission Board for final consideration.

to join the Customs Union, and this would open up possibilities for neighbouring Tajikistan in the medium-term future. Membership of the EaEU, it should be noted, is flexible and the treaty signed in May 2014 allows member states to leave of their own accord.[24]

Ultimately, the achievements of Eurasian economic integration, even at this early stage, are not confined to developing regionalism and boosting economic development, but have hinted at positive unintended consequences. One example is the contribution of the Customs Union to reducing levels of corruption.

If some producers once resorted to illegal methods to get their goods to cross-border markets, such as bribing border officials, then the removal of tariffs has alleviated this problem. The removal of internal customs controls has also curtailed opportunities for 'confiscating' goods, which was a common practice among customs officials and border guards. At the same time, the Customs Union also promises to cut red tape by enabling companies to make declarations in electronic form, and this reduction of the interface between business and bureaucracy is seen as a key to reducing corruption.[25]

Elsewhere, there is a suggestion that the top-down institutional arrangement of the EaEU can improve economic decision-making at the national level. In a region characterised by electoral authoritarianism, where loyalty takes precedence over economic efficiency, national governments lack stimuli to make effective decisions in the economic sphere. There is some optimism that the EaEU can have a trickle-down effect, where competition 'from above', in particular among the three heads of state, but also within the Eurasian Commission, will spur national governments to develop better policies.

Deepening and widening the Union

Deepening and widening the Union are seen as key directions for the EaEU by all member states, although it is fair to say that ongoing problems in both areas underline the enormity of the integration task. In some cases, the rapid progress seen since 2010 has exacerbated these problems, leaving little time to define institutional competencies. A good example can be seen in the form of the Commission's existing Regulatory Impact Assessment (RIA) procedures designed to give feedback on Commission legislation which, to date, remain weakly elaborated. There are also problems with non-tariff barriers, which although used by all regional trade blocs as a way to prevent goods from entering a territory from a third country, are presently used by Customs Union member states against each other. As with perfecting RIA procedures, resolving the problem of non-tariff barriers is essentially a question of time and, in this case, unifying the technical and safety standards between member states.

However, in some areas, the challenge of deepening the Union is a little more complex than elaborating better procedures at the supranational level. As the experience of the EU has shown, deeper integration, including the removal of non-tariff barriers, has been largely achieved on the strength of supranational institutions.

However, EaEU institutions continue to privilege national over supranational decision-making. For example, the Eurasian Commission enjoys limited supranational powers because Commission decisions can be vetoed by one country at the level of minsters/heads of state. As such, the Commission functions as a true supranational organ only when there

24 See Article 118 of the Union Agreement, Evraziiskaya Ekonomicheskaya Komissiya, 2014.

25 The so-called 'single window principle', where all documents related to an economic activity are located together in electronic form, promises to speed up business transactions once fully implemented in Kazakhstan and Russia. In Belarus, the system is already widespread.

is full agreement on an issue among member states and is closer to an 'intra-governmental' organ than a 'supra-national' body. Not only is there a danger that expansion of the Union will increase the risk of vetoes deadlocking the integration process, but there is some doubt that the supranational component of the EaEU is strong enough to overcome the historical problem of implementation seen in previous stages of post-Soviet economic integration.

In short, the future of Eurasian integration is very much conditioned by the extent to which member states, represented by the heads of state in the Eurasian Supreme Council, are able to harmonise their economic and political interests. As all important decisions are passed up the chain of command, from Eurasian Commission Board to Commission Council to Supreme Council, there are ample opportunities to defend national interests. Even if the Commission decides to pursue infringement procedures against a member state via the Eurasian Court, they must simultaneously notify the Supreme Council, opening up the possibility of lengthy behind the scenes bargaining between heads of state.

In these terms, the idea that the EaEU is doing what the EU did in a fraction of the time fails to take into account the qualitatively different logics of implementation. The Eurasian Commission may monitor enforcement in member states, but compliance with any decision will only happen if the heads of state in the Eurasian Supreme Council agree on an issue and then give the signal to their national bureaucracies to implement. Then, there is the classic principal-agent problem of bureaucracies ignoring these signals, as well as the role of weak formal institutions, notably the rule of law, in putting them into effect.

At a deeper level, implementation is also slowed by the fear among some member states of liberalising too fast. This fear is particularly evident in the case of Belarus, which despite possessing an export-oriented economy that requires integration with other markets to prosper, lags behind the other member states on most economic measures of note. Small and medium businesses lack competitiveness compared to Russian and Kazakhstani rivals and are poorly positioned to take advantage of the scale effects of the enlarged market. Belarus's economy is also heavily subsidised by the state and is the least liberal of the three existing members, creating certain contradictions in terms of Minsk's attitude to the EaEU.

What this means is that even before the EaEU formally appears in January 2015, there is a situation of multi-speed integration, both between member states, but also in the degree to which the four freedoms are being realised. So far, only two of the four economic freedoms – the free movement of goods and people – are close to being realised, but both have problem areas.

Currently, there are a number of goods that are not subject to free trade. These goods are typically labelled 'sensitive' because member states are reluctant to open their markets to competition in these areas. The alcohol and tobacco sectors are prime examples due to different excise rates in the three member states and the amount of tax revenue they generate, but medicine and pharmaceuticals can also be added to this list.

In terms of the free movement of people, one of the most pressing issues relates to the ability of entrepreneurs to register a company and then bring in labour and personnel from other member states. Residency is an issue because citizens are obliged to pay taxes in the country where they are registered, rather than the location of their economic activities. The opportunity for Russian companies to relocate to either Kazakhstan or Belarus and take advantage of lower tax rates, wage levels and production costs is currently hindered by existing residency requirements.

Elsewhere, the free movement of services and capital is unlikely to be realised in the foreseeable future. Kazakhstan was able to negotiate an opt-out for liberalising transportation services to protect domestic carriers. There is still no non-discriminatory access to the Russian gas-transport system for Belarusian and Kazakhstani suppliers, and only by 2025 is a common energy market envisaged that will finally resolve this problem. Although there are plans to create a regulative body to coordinate standards for a common financial market, the latter is not envisaged before 2025. Currency union is also seen as unrealistic by member states at this juncture, although if it were to happen, then transferring the financial centre to Astana would seem a logical concession, in view of the fact that the Eurasian Court is located in Minsk and the Commission in Moscow. However, this step would almost certainly produce a negative reaction from Russian business, further complicating the process.

In fact, the subject of establishing a single currency, as well as a Eurasian Parliament, has surfaced repeatedly since 2010, but usually in the form of a sharp rebuttal on the need for either in the format of the EaEU. This relates to the second, inter-connected problem of deepening and widening Eurasian economic integration – politicisation – and the strong desire, particularly in Belarus and Kazakhstan, to keep this project focused purely on economic goals and to reduce the political component to its bare minimum. The name Eurasian Economic Union, with the emphasis on *Economic*, is no accident, but reflects a widely held belief that business and economic interests will always find a common language, but as soon as a political component is introduced, dialogue becomes strained.

This does not mean that the political component in Eurasian economic integration is totally absent. For every member state there is a combination of political and economic considerations that are driving the integration process. For both Belarus and Kazakhstan, the economic considerations are primary. Economic union is seen as a way to modernise and improve competitiveness as well as strengthen sovereignty by creating barriers for other actors in the region, notably the EU and China, to limit the economic threat posed by 'external' powers. However, the threat to sovereignty is not only economic. As events in Ukraine in 2013/2014 demonstrated, the 'European choice' carries an existential political threat for elements of the post-Soviet ruling elite, and China, for all its economic clout, is still viewed in much of the post-Soviet space with suspicion. In many ways, Eurasian integration is an affirmation of strong, centralised power and a means to limit external interference in domestic political affairs from outside actors promoting a qualitatively different set of values.

However, when it comes to the Russian state, there is a widespread belief that, unlike Belarus and Kazakhstan, the political component driving integration is much stronger. Although access to the smaller markets of Belarus, Kazakhstan and even Armenia is not insignificant, integration is presently costing Russia more than the accrued benefits. Russia heavily subsidises Belarus and Armenia, and has already promised 1.2 billion USD to help Kyrgyzstan restructure its economy ahead of Custom Union membership.[26] For these reasons, economic motivations are seen as secondary for Russia.

Although the exact nature of Russia's motivations for integration are open to speculation, in essence, and aside from Putin's desire to assert his credentials as a regional leader capable of overseeing big regional initiatives, Russia is pursuing Eurasian integration to secure a market share in the region ahead of competing actors, namely the EU and China, in what is clearly a fight for political influence too. Russia also sees Eurasian integration as a way to counter US influence and to create a multipolar world with the Eurasian space/civilisation as one of the poles. The upshot is that despite

26 For information on Russia's financial assistance to Kyrgyzstan, see Vedomosti 2014, and for a more general discussion on the economic costs of the Union for Russia, see Knobel 2014.

attempts to limit the political component, the EaEU is an inherently politicised union from the outset. At present, this politicisation is most readily seen in the question of enlarging the Customs Union and the EaEU, and in the different approaches of the three member states towards new members.

Both Belarus and Kazakhstan stand against rapid expansion or expansion as an end in itself, and both emphasise the importance of uniform economic criteria for admitting new members. Belarus supports the principle of enlargement as a way to increase the weight of the Union on the international stage, but also understands that new members may create problems for domestic producers, depending on the conditions of membership.

Armenia, which like Belarus has a share of the Russian agricultural produce market, was granted a transitional period to implement Customs Union requirements because of pre-existing WTO commitments. This has already raised concerns in Belarus that Armenian producers will have a competitive advantage.

For Kazakhstan, enlargement should be economically beneficial for member states and should not damage relations with third countries. The problem is that both Armenia and Kyrgyzstan are failing to meet these criteria. In the case of Kyrgyzstan, the problem is mainly economic. The country has a GDP per capita of just 1,263 USD and the Central Asian republic is a key transit hub for the re-export of cheap Chinese goods, which poses a direct threat to Kazakhstani producers.

Although Armenia's economic situation is not much better, there are additional problems with borders. Not only does Armenia not have a common border with any Customs Union member state, but as no member state acknowledges either the independence or the annexation of the break-away region of Nagorno-Karabakh, Armenian membership of the Customs Union could not include the former.[27] More importantly, Armenia's inclusion in the Customs Union and EaEU complicates Kazakhstan's multi-vectored foreign policy, which emphasises good relations with regional partners such as Turkey and Azerbaijan – both of which have strained relations and closed borders with Armenia.

Ultimately, in the absence of clear economic criteria for incorporating new members, there is a concern that EaEU expansion will be driven solely by Moscow's desire to secure influence in certain regions. Armenia's surprise decision announced in September 2013 not to sign an Association Agreement with the EU and to pursue a 'Eurasian' path of integration was the result of direct pressure from Moscow and the latter's view of the South Caucasus as a key zone of influence. One danger of politically motivated expansion is that it will weaken the economic potential of the Union. Another danger is that Belarus and Kazakhstan will seek to use Moscow's politically motivated desire to expand the Union to negotiate further opt-outs and thus slow the integration process.

Conclusion: A break with the past?

Any forecast of the future of the EaEU is complicated by a number of factors, not least the mood of optimism surrounding the signing of the treaty on May 29 and Armenia's expected accession to the Customs Union. There is also clear evidence that the EaEU represents a more serious phase of post-Soviet economic integration and that, for the time being, the commitment of member states ensures that the EaEU will be more than 'ink on paper'.

27 There is also an issue with the porous de-facto border between Nagorno-Karabakh and Iran that could see goods enter Customs Union territory illicitly. Kazakhstan, it should be noted, is also uncomfortable with the potential incorporation of unrecognised states into the Customs Union and EaEU, such as South Ossetia and Abkhazia, but also the newly annexed Crimea.

However, the problems highlighted in the previous section are by no means easy to resolve, mainly because they have been fundamental to both the success and failure of post-Soviet economic integration over the past two decades. As argued in this report, the latest phase of post-Soviet integration shows strong signs that the previous path dependency has not been broken, and that weak institutions and the large asymmetry that exists between member states are continuing to hinder economic union.

The problem of implementation and multi-speed integration really relates to the longer-term issue of weak institutions. In a somewhat counter-intuitive way, weak supranational institutions have created flexibility, allowing member states to move towards each other at their own pace. This can be seen in a number of areas, not least the agreement on the Customs Union Code, which owing to the sheer number of disagreements between member states resulted in the prevalence of reference rules, left to the discretion of national customs bodies to resolve. Although this was not ideal, it was the quickest, perhaps only way to reach agreement.

Weak institutions at the national level and the absence of effective democratic checks and balances have also enabled the leaders of the three member states to make important decisions without the need to engage in lengthy public consultation or bargaining to obtain parliamentary approval. The overall institutional design of the EaEU, with real decision-making located in the Supreme Council, means that the three heads of state can decide to take integration in different directions, to develop stronger supranational bodies in the future, should that avenue become expedient.

However, weak institutions, while being a short-term asset, create longer-term problems in achieving deeper integration. There is an opinion expressed in some quarters than since everyone is trying to bypass the rules and since the means to enforce them are so weak, it becomes normal behaviour to simply pretend to honour obligations. At the same time, although the advantage of the three-president model of integration is that it speeds up decision-making, the quality of this decision-making is reduced to the qualities of just three individuals. The weakness of domestic political institutions in facilitating real public involvement, combined with the weakness of formal mechanisms to manage leadership change in each member state, make the Eurasian Economic Union prone to rapid revision in a way quite unlike most other regional integration projects.

As for politicisation, this really relates to the older problem of asymmetry and the fear that too much integration will result in a loss of sovereignty for smaller member states. In effect, Belarus and Kazakhstan see a tipping point in the integration process – at a certain level, integration enhances sovereignty, but too much of it creates a threat. This is the deeper issue at play in the differing attitudes towards incorporating new members. As well as the need to balance regional partners and maintain multi-vector foreign policies, there is a fear that Russia will use new client-member states, notably Armenia, to pressure Kazakhstan and Belarus on certain issues, in effect giving Russia an additional vote in the Supreme Council. The reluctance to follow Moscow's lead on all issues was also seen in June 2014 with Russia's failure to convince Belarus and Kazakhstan to support the proposed EaEU-wide sanctions against Ukraine.

For Kazakhstan, asymmetry is part of the reason why Astana wishes to slow certain aspects of integration. For example, realising the four freedoms will take time, not because they are considered unimportant, but because of the fear that bigger Russian companies stand to gain from rapid liberalisation. Services, for example, in particular in the insurance and banking sector, will take time to liberalise precisely because of this perception of asymmetry.

For Belarus, there is a similar concern that Russian companies with their capital and business acumen will take advantage of liberalisation to swallow up domestic companies. Not only is there the threat of illegal take-overs in the form of *reiderstvo*, which are common in Russia, but also through more subtle ways, such as manipulating shareholders to change company management in favour of Russian interests.[28]

As with weak institutions, asymmetry has often helped to push integration. Russia has successfully used its economic asymmetry in recent years to gather states around it and to harmonise interests, but the obvious drawback is that the success of the EaEU now depends to a large extent on Russia's economic performance. Economic stagnation could see subsidies for members like Belarus dwindle to a survival minimum, with largely unpredictable results, serving to speed up liberalisation or halt it altogether.

It is in this context that the EaEU and its member states must find a way to realise the undoubted potential of Eurasian economic integration and to build on the successes already achieved. The key task is to find a balance so that the weakness of institutions and the asymmetry that exists within the Union continue to push integration rather than slow its progress. In the meantime, regional integration never occurs in a vacuum, and so the role of international factors should not be underestimated. The impact of the Ukraine crisis on the EaEU is likely to be far-reaching, not least because Ukraine's participation in the Union was a major objective for the EaEU to begin with. With Russia's relations with the West already being described in terms of a new Cold War,[29] and with Russia facing formidable structural economic problems, the future of Eurasian economic integration looks less certain going forward.

In short, the easy part of integration has already been achieved, and what comes next, seen in terms of deepening, widening and stimulating economic development, will be harder to secure. From this perspective, the salient question surrounding the Eurasian Economic Union is not whether it will succeed in achieving EU-style integration in a fraction of the time, to present itself as a partner or a rival in the region, but whether the latest intensive phase of post-Soviet economic integration, seen since 2010, will slip into a dormant phase, where early gains and paper agreements mask a very different reality on the ground.

28 *Reiderstvo* is a form of asset-grabbing. The problem is acute in Russia, where criminal gangs, often in collusion with the courts and security services, eject owners of businesses by force and forge documentation to claim ownership.

29 Trenin, 2014.

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APPENDIX 1: LIST OF INTERVIEWEES

Below is an alphabetical list of interviewees, grouped by country. As stated in the introduction, this report does not constitute the views of every participant, but reflects the balance of opinion expressed by all interviewees.

Belarus (Minsk)

Roman Brodov, Head of Foreign Economic Policy Division, Ministry for the Economy

Vitaly Busko, Professor, member of the House of Representatives (Lower House of the National Assembly), Deputy Chairman of the Standing Commission on International Affairs

Alexander A. Filippov, Professor, Head of the Youth Affairs Department, Belarusian State University of Culture and Arts; previously expert with the Information-Analytical Centre of the Administration of the President (2010–2013)

Alexander Guryanov, Deputy-Minister for Foreign Affairs

Vladimir Kariagin, Chairman of the Association 'Minsk Capital Union of Entrepreneurs and Employers', president of the Belarusian Republican Confederation of Entrepreneurship (RCE)

Lev E. Krishtapovich, Deputy Director of the Information-Analytical Centre of the Administration of the President

Andrei Rusakovich, Professor, Belarus State University, Head of the Foreign and Security Policy Studies Centre

Vladimir Ulakhovich, Deputy Chair of the Chamber of Trade and Commerce of Belarus

Kazakhstan (Astana & Almaty)

Aidar Amrebayev, Head of the First Kazakhstani President Center, Institute of World Economics and Politics at the Foundation of the First President of the Republic of Kazakhstan

Tulegen Askarov, President of the Center for Business Journalism BizMedia

Ernar Bakenov, Director of the Department of International Economic Integration, Ministry of Economics and Budget Planning

Murat Karimsakov, President of the Eurasian Economic Club of Scientists Association (EECSA)

Nargis Kassenova, Director of Central Asian Studies Center, KIMEP University

Asan Kozhakov, Ambassador-at-Large, Ministry of Foreign Affairs

Darya Mukhamedjanova, Chief Research Fellow, Economic Studies Department, the Kazakhstan Institute for Strategic Studies (KISI)

Askar Nursha, Coordinator of Projects on Foreign Policy Issues, Institute of World Economics and Politics at the Foundation of the First President of the Republic of Kazakhstan

Dosym Satpayev, Director of the Risk Assessment Group

Alma Sultangalieva, Advisor to the Director, Institute of World Economics and Politics (IWEP) at the Foundation of the First President of the Republic of Kazakhstan

Russia (Moscow)

Rustam Akberdin, Director of the Department for Development Entrepreneurship, Eurasian Economic Commission

Askar Kishkembayev, Head of the Secretariat of the Minister for Economy and Financial Policy, Eurasian Economic Commission

Aleksandr Knobel, Laboratory of International Trade, Gaidar Institute for Economic Policy

Andrey Kortunov, President of the New Eurasia Foundation; Director of Russian International Affairs Council (RIAC)

Valentina Kravchenko, Deputy Director of the Department for Financial Policy, Eurasian Economic Commission

Dmitry Polyanski, Deputy Director, First Department of CIS countries, Ministry for Foreign Affairs

Natalya Postnikova, Senior Research Fellow, Gaidar Institute for Economic Policy

Gulnur Rakhmatullina, Minister for Economic and Financial Policy, Eurasian Economic Commission

Amirbek Sankubayev, Head of the Financial Market Division, Eurasian Economic Commission

Vitali Survillo, Vice-President of All-Russia Public Organization Delovaya Rossiya

Natalya Volchkova, Lead Economist, Centre for Economic and Financial Research (CEFIR)

Armenia (Yerevan)

Alexander Arzoumanian, Deputy of the National Assembly of Armenia, Deputy Chair of the Foreign Relations Committee

Richard Giragosian, Director of the Regional Studies Center (RSC)

Robert Harutyunyan, Director of Armenian Development Agency, Ministry for the Economy

Alexander Iskandaryan, Director of the Caucasus Institute

Vahagn Khachatryan, Economist, the Armenian National Council

Aram Manukyan, Deputy of the National Assembly of Armenia, member of the European Integration Committee

Aghvan Vardanyan, Deputy of the National Assembly of Armenia, Chair of the Gas Supply Committee