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Common Economic Space: another step towards integration focused on Russia

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On 9 December in Moscow, the Presidents of Russia, Dmitri Medvedev; of Belarus, Alyaksandr Lukashenka; and of Kazakhstan, Nursultan Nazarbayev, signed a declaration on the establishment of a Common Economic Space (CES) and a set of agreements on how this structure will function. The CES is planned to come into operation on 1 January 2012 and, in accordance with Russian announcements, to lead to the creation of a common market (based on four freedoms: the free flow of goods, services, capital and labour) within this area, on the model of the European Communities.

On one hand, the adopted documents concerning the CES are quite general in nature; among other reasons, this is due to the fairly large discrepancies in the signatories' interests. They therefore require some refinement – and this calls into question whether the declared objectives can be fully implemented. On the other hand, , all the members of the Community are looking for certain political and economic benefits from this project, which weighs in favour of closer cooperation. Consequently, we can expect that the convergence of the economies of Russia, Kazakhstan and Belarus will be a lengthy and difficult process, which will lead to only a partial economic integration between the partners.

The general principles of the Common Economic Space

The Common Economic Space is the next step in the integration of Russia, Kazakhstan and Belarus, which since 1 July 2010 have made up a Customs Union. The original plan for the CES, which was less ambitious and specific, appeared in 2003 in a group which then also included Ukraine. However, Kyiv did not ratify the agreement on the CES, which led to the collapse of the project in 2006. In December 2009 Russia, Kazakhstan and Belarus returned to the negotiations, and prepared a plan to create this Community. The CES's current legal basis consists of 17 agreements principally concerning all aspects of the partners' economic life (for more details see the Appendix). These documents should be ratified by the parliaments of the three countries by the end of this year. One impetus for Minsk to ratify is the fact that duty-free supplies of Russian oil to Belarusian refineries are dependent on this.

The agreements constituting the CES's legal basis serve to establish the three states' comprehensive economic integration. It should unify most technical and legal regulations, monetary policy, public support for the economy, and access to natural monopoly services (see Appendix). At the same time, the parties have set themselves very ambitious

timeframes for implementing these goals (namely, during 2011), with only some matters to be settled within three-year transitional periods (the CES is to operate fully as of 2015). The final versions of these documents have not yet been published. From the descriptions which have appeared in the media, it appears that some of the plans became less specific during the negotiations (for example, the plan for the phased reduction of state participation in specific spheres of the economy was dropped in favour of simply describing this as a goal). In addition, the partner countries were given the rights to exemptions and to the use of national regulations (including on migration policy). The parties were probably unable to develop an effective mechanism for settling disputes, which may prove a serious limitation to implementing the agreements.
Despite these limitations, the parties have decided to sign the agreements on the CES because of the economic and political benefits they expect to obtain from them.

Russia's interests

For Russia, closer cooperation on the territory of the former Soviet Union is both an economic and a geopolitical project. On the one hand, it is Moscow's response to the integration processes taking place elsewhere in the world (such as the free trade area proposed by the European Union to Eastern European countries, and China's similar proposal to the Central Asian states). The creation of this Community, therefore, is aimed at counteracting the economic expansion of third countries and loosening their economic links with Russia. In the period from 2000 to 2008, the share of exports from Kazakhstan and Belarus to the Russian Federation in these countries' total export trade decreased by 11 percent (to 9%) and 18 percent (to 32%) respectively.
By creating the CES, Russia seeks to further expand the markets for its goods (integration on Moscow's conditions will increase the competitiveness of Russian goods on its neighbours' markets, especially cars, machinery and equipment) and to control the transmission of raw materials from the region.
On the other hand, deepening integration with Belarus and Kazakhstan is part of the Russian vision of a Greater Europe – the creation of an integrated economic area covering the area of the European Union, Russia and its neighbours. This vision was recently presented in Berlin by Prime Minister Vladimir Putin. By strengthening and solidifying its neighbours' interdependency, Russia may act as the representative of the entire bloc of countries (Kazakhstan and Belarus) in its relations with the EU, which will strengthen Moscow's position towards Brussels. For this reason Russia is also now especially concerned with making its model for integrating the region's other countries appear convincing, especially to Ukraine (which is currently uninterested in this project). This would significantly increase the potential of the CES, and hence its importance. By moving towards the creation of the CES, Moscow is working to present it as an attractive plan for integration in this region.

Kazakhstan's interests

Kazakhstan also sees the CES mainly in geopolitical terms. This project's importance is demonstrated by the active support it has received from President Nursultan Nazarbayev.

Astana is aware that it is too weak to withdraw from cooperation with Russia (which is the largest supplier of goods to Kazakhstan), or to resist the growing influence of China on its own. For Kazakhstan, deeper economic integration with Russia is therefore a form of defence against Beijing's economic expansion, and a counterbalance. In this context, the CES is seen as a tool that will help to channel cooperation with China, and give it the form Kazakhstan desires (this includes protecting it against a flood of cheap Chinese products).
Moreover, Astana sees the CES and the opening of the borders with Russia (the investment climate in Kazakhstan is regarded as the most attractive of all the CES states) as a chance for an increase in foreign investment. It also hopes to become a production base for the region as a whole, which the creation of the Khorgos special economic zone on the border with China is intended to serve.

Belarus's interests

For Minsk, signing the CES documents is primarily a way to step back from confrontation with Moscow. In this way, the Belarusian government will avoid the risk of a total halt to energy and economic subsidies. By joining this structure, Belarus has obtained guarantees that its concession prices for raw materials will continue, including duty-free supplies of Russian crude oil (which may mean oil subsidies of around US$2bn per year from the Russian budget). Access to Russian market outlets is also very important, as it is a precondition for the survival of a significant part of Belarusian industry (Russia receives over 90% of Belarus's food production exports, and on average 70% of its machine production exports). Minsk is also hoping that the CES's plan for free movement of goods and services will make investing in Belarus more attractive. Besides, the Belarusian government has concluded that accepting Russian legislation which complies with the World Trade Organisation (WTO)'s requirements will give it the chance to join the WTO itself.

Conclusions and forecasts

The documents signed are largely general in nature. It will thus be necessary to agree upon the details and the executive acts for the agreements. Moreover, the partner states still have conflicts of interest in certain areas (such as access to markets for sensitive goods, i.e. oil, gas, cars, and agricultural products; subsidies for industrial production in the form of low energy prices; the work force's access to the labour market; the expansion of Russian capital into the Belarusian energy sector). It therefore seems unlikely that Russia, Belarus and Kazakhstan will fully achieve their objectives (freedom of movement for goods, services, capital and labour) by 2015. None of the parties is ready to remove (or appreciably restrict) real control over its own economy. Consequently, further unilateral decisions by the CES states to protect their own markets should be expected; examples of this are the Russian embargo on grain exports; Kazakhstan's ban on exporting oil products; and the export duty imposed on supplies of Russian gas to Belarus. From this perspective, the CES may in fact create new areas of conflict, mainly in Russian-Belarusian relations.
Although we should not expect integration at the speed and style which the members of the CES have declared, their real determination and their national interests (especially those of

Russia) mean that some of these plans will be implemented; this will facilitate the movement of goods or certain services between the partners. Integration within the framework of the Community to a great extent means adapting the region's economic laws to those of Russia, which will undoubtedly limit opportunities for Belarus and Kazakhstan to engage in integration projects which bypass Russia (such as Belarus starting discussions with the EU on forming a free trade zone in the future).
The CES countries' determination to succeed shows that the total failure of this integration would mean Russia's further displacement from its region of economic and political influence by China, the European Union and the USA; for Kazakhstan, failure would mean the threat of economic dependency on China; and for the government of Belarus, there is the threat that its present economic model, which is based on preferential prices for Russian energy materials, would collapse.

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Appendix

The main elements of the CES's agreements

The main body coordinating the day-to-day functioning of the Common Economic Space is to be the Customs Union Commission, which already exists within the framework of the Customs Union. It includes the Deputy Prime Ministers of Russia, Igor Shuvalov (who is head of the Commission); of Belarus, Andrei Kobyakov; and of Kazakhstan, Umirzak Shukieyev. This Commission drew up the 17 agreements on the principles of the CES's functioning. These concern the following:

1. **the development of a common economic policy**, including:
– macroeconomic policy assumptions, including the determination (based on the model of the EU's Maastricht criteria) of maximum permissible levels of inflation, public debt, budget deficit and interest rates;
– regulations for selected natural monopolies, but excluding the markets for gas, electricity, heat, pharmacological, petroleum & alcoholic products, and nuclear energy, among others;
– regulations of competition, as the parties withdrew from a plan to gradually limit state participation in specific spheres of the economy, in favour of a declared intention to reduce the number of enterprises with state participation to 10% in the year 2015;
– principles of state subsidisation of industry and agriculture;
– public procurement, by means including the preparation of lists of goods or services which may be procured without tender;
– regulations for trade in services and for investment policy (although the parties decided that these issues will mostly be regulated by the national law of each country);
– regulations for protecting intellectual property.

2. **freedom of movement for capital, and a common monetary policy** (although the introduction of a single currency is not yet anticipated);

3. **energy, transport and communications**, including the organisation, management, operation and development of a common market for oil and petroleum products, as well as access to services and the development of prices and tariffs in electrical energy, the transport of gas, and railway transport;

4. **freedom of movement for the work force**, including tackling illegal migration from third countries and determining the legal status of migrant workers and their family members (the parties decided that these issues will mostly be regulated by the national law of each country);

5. **the unification of technical standards**.