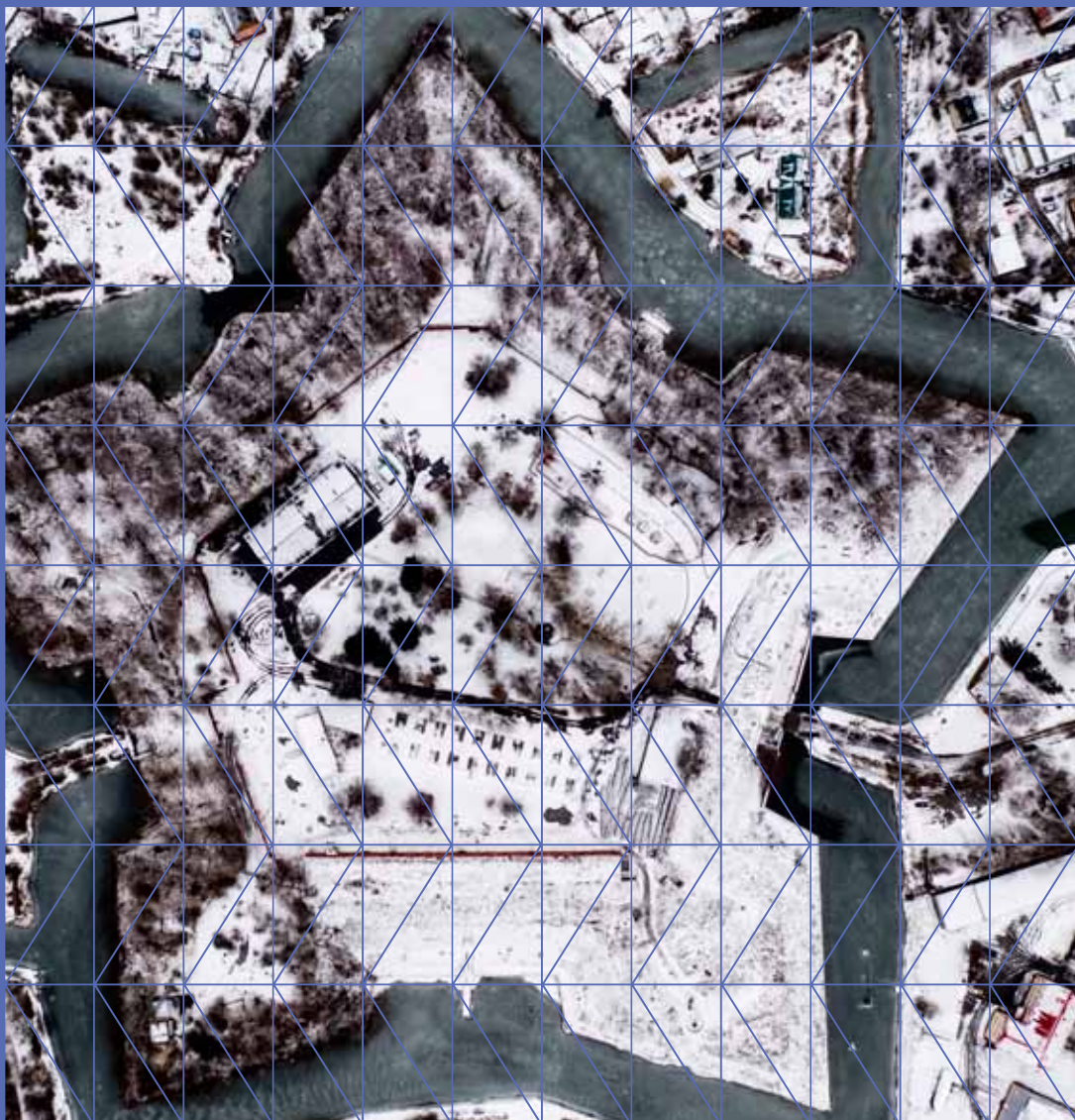


OSW REPORT

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FORTRESS KALININGRAD

EVER CLOSER TO MOSCOW

OSW Team

WARSAW
OCTOBER 2019

FORTRESS KALININGRAD

EVER CLOSER TO MOSCOW

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MAIN POINTS

- Moscow's policy towards the Kaliningrad Oblast has been increasingly consistent in recent years. Its main objective has been to further tighten its grip on the region and its links to mainland Russia in the political, social and economic dimension. As a result, the Kaliningrad Oblast has been made more subordinated to Moscow, which is in line with a general trend in the relations between Russia's central government and the regions.
- In 2017 Anton Alikhanov, a Moscow designate, formally confirmed his political mandate to hold the position of the governor of the Kaliningrad Oblast in elections which were *de facto* non-competitive. Alikhanov has since dismantled the pre-existing political and business structures in the oblast and rid himself of political competitors. Power in the region has become centralised and concentrated in the hands of the governor. However, Alikhanov's role is that of a caretaker tasked with safeguarding the regional interests of actors with close links to the Kremlin. In some cases these clash with the interests of the regional elite.
- Public sentiment in the oblast regarding social and economic issues has been consistently deteriorating, but this has not generated much protest activity. The people and the regional elite seem to be passively accepting Moscow's policy and Governor Alikhanov. The political opposition in the region remains weak and divided. However, many grassroots social initiatives are still active in the oblast, most of them apolitical and focused on the protection of cultural heritage or the environment and on cultural or charitable activities. On Moscow's initiative, efforts have been made to suppress this social activity and undermine the Kaliningrad identity – including a campaign to counter 'Germanisation'. However, despite the region's unique geopolitical position and efforts by the special services to promote the 'besieged fortress' narrative, the level of repression in the oblast is similar to the Russian average.
- The improved economic conditions in Russia and the influx of federal funds into the region in connection with the organisation of the 2018 World Cup and other projects, have boosted the Kaliningrad Oblast's macroeconomic performance, especially during the last two years. However, the public has not benefited from the economic growth as real incomes continued to decrease, following the trend seen for several years. As a result, the standards of living in the oblast have been declining and are below the Russian average.

- The Kremlin has stepped up control of the region's economy by making its revenues even more dependent on transfers from the federal budget and increasing the presence of federal companies implementing large projects related to the expansion of the energy infrastructure (new power plants, the floating LNG terminal) and the regional transport infrastructure (the expansion of ports, the airport and ferry links). Those projects, which mainly benefited people from President Putin's inner circle, increased the region's self-sufficiency and in this way made it even more isolated. This contrasted with the Kremlin's activities to foster co-operation with the neighbours, such as the creation of a transport and logistics centre, plans to promote tourism (e.g. by introducing electronic visas) and cross-border co-operation projects.
- Despite Russia's worsening political relations with Poland and Lithuania, dialogue at the regional political and local-governmental level has continued. Cross-border co-operation projects co-financed by the EU under the 2014–2020 budget are being implemented.
- Kaliningrad residents are very mobile – the percentage of people holding passports is twice as high in that oblast as the Russian average. People from Kaliningrad Oblast travel most frequently to the neighbouring EU countries, drawn by the lower prices and better quality of products. However, the intensity of travel to Poland and Lithuania, and the volume of purchases in those countries, have decreased recently, mostly because of the depreciation of the rouble (after 2014) and the suspension (in 2016) of the local border traffic regime which made crossing the border with Poland easier and less expensive.
- As tensions in Russia's relations with the West increased, the Russian special services have stepped up their defensive and offensive activities in this region whose location Moscow regards as strategic. Defensive activities have been focused on preventing a further loosening of the oblast's links with Russia, while offensive activities involved monitoring and countering NATO's activities, as well as political lobbying. The reshuffles in the regional directorates of the institutions of force have been aimed at strengthening discipline and reigning in corruption schemes or taking control of them.
- Russia has stepped up efforts to modernise and expand its military potential in the Kaliningrad Oblast, achieving a noticeable improvement of the

offensive capabilities of the Kaliningrad-based units of the Armed Forces of the Russian Federation. Those efforts have involved:

1. expanding military infrastructures (including the expansion of the military airfield and upgrades of nuclear weapons depots),
2. increasing the presence of military personnel (including the re-activation of a tank regiment and a fighter aviation division),
3. further technological upgrades (including the permanent deployment of the Iskander missile systems, expansion of the coastal defence Bastion missile systems, deployment of additional fighter aircraft, helicopters, tanks and warships), and
4. increased training activities (including drills with offensive scenarios).

The Russian air force and navy based in Kaliningrad have also continued to stage provocations against the forces of NATO countries.

Map 1. Kaliningrad in Europe





INTRODUCTION

The Kaliningrad Oblast is a Russian exclave separated from the Russian Federation by the territories of Poland and Lithuania (both of which are EU and NATO member states) and of Belarus. It is the only part of Russia that has a border with Poland and Lithuania. Its geopolitical location makes Kaliningrad Oblast an important Russian outpost in the northern part of Central Europe. It is therefore strategically important for Russia, as well as for Poland and Lithuania and the entire region. For this reason, the Centre for Eastern Studies (OSW) considers monitoring the political, social, economic, energy, security and military situation in the Kaliningrad Oblast to be one of the priority areas of its analytic work.

In recent years OSW has published two major studies on the Kaliningrad Oblast: in 2012 it published: *A captive island: Kaliningrad between Moscow and the EU* as part of the “OSW Studies” series, and in 2016 it followed up with the report *Kaliningrad Oblast 2016. The society, economy and army*. Because important new developments have taken place in the Kaliningrad Oblast between 2016 and 2019 in the political, economic and military dimension, OSW decided to produce a new report on the subject.

The purpose of the present paper is to analyse the most important changes that have taken place in the Kaliningrad Oblast since the publication of the last report. Therefore, the present report will not repeat basic information about the region which was provided in the previous reports. It will instead focus on an in-depth analysis of how the situation has evolved in the different dimensions that are of interest here. The text is divided into four parts.

Part One analyses the dynamics of the political and social situation with special focus on: changes in the relations between the federal centre and the oblast; the situation within the power elite; and the development of civil society activities.

Part Two is devoted to analysing the economic situation and looks in particular into social and economic indicators and the evolution of Moscow’s policy towards the region, including its transport and energy projects.

Part Three delves into the oblast’s relations with the external world, including its cross-border contacts and co-operations, the movement of people and economic exchange.

Finally, Part Four is devoted to the evolution of the internal security situation and policy, and the expansion of Russia's military potential in the region. Appendices with additional detailed data on selected topics complement the text.

One aim of the report is enhance the knowledge which Polish and foreign audiences have about the situation in the Kaliningrad Oblast and its role in the policy of the Russian Federation. A further aim is to contribute to a wider analysis of Russia's policy and public debate on this subject.

Interesting facts about Kaliningrad

The Polish poet Jan Kochanowski (1530–1584) visited the Albertus University of Königsberg (Albertus-Universität Königsberg) in the years 1551–1552 and 1555–1556.

The first book in Lithuanian – The Catechism (*Katekizmo paprasti žodžiai*), authored by Martynas Mažvydas, was published in Königsberg in January 1547.

The German philosopher Immanuel Kant (1724–1804), who was born and lived in Königsberg, swore allegiance to the Empress Elisabeth of Russia after the Russian army seized the city in 1758 in the course of the Seven Years' War. When the province was restored to Prussia four years later, Kant did not want to retract his oath and formally remained a Russian subject till the end of his life.

The Königsberg castle is where the original Amber Room was last seen.

Between April 1945 (capture by the Red Army) and July 1946, Kaliningrad bore the Russian version of its previous German name: Königsberg (*Кёнигсберг*). In April 1946 the Königsberg Oblast of the RSFSR was created (renamed as the Kaliningrad Oblast in July 1946).

Mikhail Kalinin, after whom the oblast's capital was named in 1946, never visited the city of Kaliningrad or the region. As the president of the Soviet Union's Supreme Soviet (1938–1946), Kalinin was co-responsible for mass crimes – his signature can be found on hundreds of execution lists including the Katyn execution list. In the years 1931–1990, the city of Tver was named Kalinin. Tver is the capital of the Tver Oblast where in 1940 the NKVD murdered 6,300 Polish prisoners of war who were subsequently buried in Mednoye.

The Kaliningrad Oblast accounts for 90% of global amber reserves. According to folk medicine, amber beads worn around the neck prevent a sore throat and headaches while also keeping the thyroid healthy. The largest known lump of amber kept at Kaliningrad's Amber Museum weighs four kilograms. Also on display at the Museum is an amber mosaic titled *Rus*, which weighs more than 70 kg.

Kaliningrad has the highest number of beauty parlours *per capita* in Russia.

I. POLITICAL AND SOCIAL SITUATION AND INTERNAL POLICY

1. The political situation: balance of power in the regional elite

A qualitative change has occurred in the governance of the Kaliningrad Oblast in recent years, affecting both the internal regional governance and the relations between the oblast and Moscow. The regional elite has become much less pluralistic: the previous model in which the mayor of Kaliningrad competed for influence with the governor has been replaced by a centralised model with power concentrated in the governor's hands. The governor, however, is not an independent politician, but rather a technocratic caretaker overseeing the interests of federal political and business actors in the region. This arrangement is in keeping with the strategy which the Kremlin has been implementing for years to tighten its control of the Russian Federation's subjects.

On 10 September 2017, Anton Alikhanov, who had been acting as the region's chief since 6 October 2016, was elected as the governor of the Kaliningrad Oblast in a general election. According to available information he has links to Viktor Chemezov, the influential CEO of the state-owned Rostec corporation (Rostec owns the Kaliningrad Amber Combine). Alikhanov so far enjoys strong support from the Presidential Administration (according to some sources, he is a protégé of the administration's deputy chief in charge of its internal policy division, Sergey Kiriyenko).

Governor Anton Alikhanov

Anton Alikhanov, the governor of the Kaliningrad Oblast, was born in 1986 in Sukhumi (Abkhazian ASSR). He is a lawyer and holds a PhD in economics. He comes from a wealthy family. His father Andrey was one of the founders of Rosmyasomoltorg, a large food processing company in which he holds 20% of the shares. Andrey Alikhanov is friends with Igor Shuvalov – the former deputy prime minister of Russia, current chairman of State Development Corporation VB.RF, and Mikhail Babich – the former president's plenipotentiary in the Volga Federal District and current deputy minister of economic development.

In 2010 Anton Alikhanov started working at the Ministry of Justice, and in 2013 – at the Ministry of Industry and Trade where he served as the director of the Department for the Regulation of Foreign Co-operation (among

other posts). On 22 September 2015 he was appointed deputy prime minister of the Kaliningrad Oblast (in charge of agriculture and industry). Less than a year later, on 30 July 2016, he was promoted to the function of acting prime minister of the region, a position that was restored especially for him by the then newly appointed acting governor Yevgeny Zinichev (during the term of the previous governor Nikolai Tsukanov, the regional government was headed by the governor). On 6 October 2016, President Vladimir Putin entrusted Alikhanov with the function of acting governor of the Kaliningrad region (at the same time, the traditional model in which the head of the region heads the regional government was reinstated). Alikhanov became the youngest regional governor in recent Russian history.

In the gubernatorial elections on 10 September 2017, Alikhanov had no real competitors, and the campaign proceeded without any problems, thanks to the traditional use of the so-called administrative resource (administrative control over the campaign and voting), cooperation on the part of the 'licensed opposition', and the weakness of the actual opposition in the region. Apart from him, only technical candidates competed, including Igor Revin, a Communist member of the regional parliament, Yevgeny Mishin, a regional MP representing the Liberal Democratic Party of Russia, and Yekaterina Timofeyeva of the marginal Russian Green Ecological Party. Alikhanov officially won 81% of the vote – a record-breaking victory in the history of the Kaliningrad Oblast (his predecessor Tsukanov won 70.4% in 2015 with a similar turnout of slightly over 39%). Alikhanov's official result of 76.24% was the lowest, though still very high, in the region's capital city of Kaliningrad. According to Golos, the independent organisation which monitors the elections in Russia, violations of procedures during the counting of votes in the Kaliningrad region were 'massive' and 'catastrophic'.¹

From the start, Alikhanov's role in the Kaliningrad Oblast has been to modify the region's political governance model, i.e. to dismantle the established political and business relations, including the entrenched corruption schemes, and centralise decision making (concentrate major prerogatives in the hands of the regional executive at the expense of the municipal authorities).

The local elite was not happy when an outsider, who had never been connected with the Kaliningrad region and who probably did not intend to associate

¹ 'Выборы в Калининграде: подкуп и катастрофический подсчет', Голос, 11.09.2017.

himself with Kaliningrad in the future, was appointed to the top position in the region. The ambitious Alikhanov saw working in Kaliningrad as a kind of 'exile', but also a springboard that would allow him to return to his federal career. In the perception of the regional elites, this meant that he would only look after the interests of the region, including those of the local interest groups, as much as would be necessary to win the Kremlin's appreciation. **Moscow's interests in the region, represented primarily by Alikhanov and the security institutions, are – as in the case of other regions of Russia – often contrary to the interests of local elites, especially when it comes to defining the region's budget or controlling regional assets, including proceeds from corruption.**

In the years 2017-2018 the balance of power in the Kaliningrad Oblast's regional elite changed, mainly as a result of:

- 1. the dismissal of Nikolai Tsukanov**, the former governor of the Kaliningrad Oblast, from his position as the Russian president's plenipotentiary in the North-western Federal District (NWFD), as a result of which he lost his sway over the Kaliningrad elite and the situation in the oblast;
- 2. the dismissal of Kaliningrad Mayor Alexander Yaroshuk** (who in the past has competed for influence with successive governors including Anton Alikhanov);
- 3. to a lesser extent – the dismissals of the heads of several municipal districts in the oblast**, who held their functions before Alikhanov's term began.

The dismissal of Tsukanov in December 2017 ended his conflict with Alikhanov dating back to the latter's appointment as acting governor. As the Kremlin's plenipotentiary in the NWFD, Tsukanov indeed had less power than he used to have as the Kaliningrad governor (the function of the plenipotentiaries has increasingly been more about representation than decision-making in recent years). His ability to influence the leaders of the different regions of the NWFD was limited, but he nonetheless considered the Kaliningrad Oblast his fiefdom, not only because he was a Kaliningrad native, but also because he had left behind an extensive network of business interests, including sources of proceeds from corruption. Those business interests came under threat the moment he was forced to resign as governor in July 2016, less than a year after having won another election. Because of his concern that Alikhanov might reveal his financial abuses, Tsukanov tried to discredit him in the eyes of the Kremlin

(with allegations of, inter alia, ‘incompetence’ in social policy). According to some sources, Tsukanov was so fiercely opposed to Alikhanov’s candidacy in the governor elections in September 2017 that he lobbied in Moscow for the Kaliningrad mayor Alexander Yaroshuk, whom he disliked, to be designated as the Kremlin’s candidate. However, the priority for the Kremlin was to step up control over the economy and finances in the Kaliningrad Oblast and ensure the region’s stability. In the end the conflict was resolved by dismissing Tsukanov from his position in the NWFD (currently he serves as the president’s plenipotentiary in the Ural Federal District).

Alikhanov’s position was further strengthened by the **dismissal of the Kaliningrad mayor Alexander Yaroshuk**, an ambitious regional politician and entrepreneur, in March 2018, i.e. less than six months after he was re-elected. According to one version of events, his departure was the result of a compromise. The mayor, who was inconvenient for Alikhanov, allegedly agreed to resign after successfully completing the construction of the Kaliningrad stadium and ensuring a good result for Vladimir Putin in the region’s capital in the presidential election. In the 2018 by-elections, Yaroshuk won a mandate in the State Duma, which formally put him in a higher position and provided protection thanks to the immunity of deputies, while Alikhanov, having established himself in the Kaliningrad Oblast, had rid himself of a competitor. Alikhanov also made sure to weaken the institutional powers of the Kaliningrad mayor. On his initiative, in November 2016 the regional parliament adopted a law abolishing direct elections of the mayor in favour of election by the city council. According to Alikhanov himself, the project fitted into a “general federal trend” (indeed, in 2018 mayors were still elected in direct elections in only ten Russian cities), and its roots lay in the “long-standing rivalry between regional and municipal authorities” in Kaliningrad, “resulting in, among other things, the city’s problems with raising funds for infrastructure projects”. Thus, the mayor was not only deprived of his electoral mandate, which weakened his political importance, but has also become much more dependent on the support of the regional authorities. Unlike Yaroshuk, **the new mayor Alexei Silanov is not a political player**. He was considered a compromise candidate and accepted by all the main interest groups, which may help stabilise the sentiments within the regional elite.

Meanwhile, the power and business relations within the regional elite have visibly weakened **and regional governance has become more centralised as municipal authorities were stripped of some of their powers**, e.g. in the area of spatial development (building permits) or public procurement.

The bill on depriving the municipal level of powers in the field of construction entered into force in January 2017, so it was one of the earliest decisions of the newly appointed acting governor and was justified by the need for better urban planning and also by the need to combat corruption. A partial reshuffle has also taken place among the heads of municipal units, with the mayors of Gusev (who had close links to Tsukanov), Krasnoznamensk, Svetlogorsk and other towns losing their positions. Criminal cases were initiated (on charges of abuse and embezzlement) against the mayors of the towns of Svetly and Sovetsk.

As he stepped up control of the regional elite, Alikhanov has nonetheless pursued a balanced appointments policy as a gesture to the native Kaliningrad elites. The fears that the new governor would strip members of the regional elite of their influence in the regional administration did at first seem justified. However, Alikhanov's appointments to date rather indicate that he is taking care to entrust the highest positions to people born in the Kaliningrad Oblast or those who have been associated with the region for a long time. While the first deputy prime minister Alexei Rodin, formally responsible for regional security and the administrative apparatus (including appointments) is Alikhanov's trusted aide from his Moscow times, nearly all other deputy prime ministers and two thirds of ministers are people who have been associated with the region for years and, in many cases, have previously worked in the Kaliningrad Oblast government or in the municipal bodies. Some deputy prime ministers and ministers have been serving in their positions since the times of the previous governors.

Alikhanov has probably been so careful in navigating his way among the regional elite for two reasons. Firstly, his personal and professional ambition is to prove his worth in front of the Kremlin as a successful leader of a difficult region of crucial geostrategic importance and the one remaining under tight control of the secret services. Secondly, like many other 'technocratic' governors appointed in recent years, Alikhanov is not a political player but rather a medium-level nomenklatura manager with little independence in governing the region. The two main tasks that the Kremlin expects the governors to achieve concern subduing conflicts within the regional elites and ensuring social peace. Both require governors to enjoy at least the neutrality of the most important regional interest group leaders.

In the logic of the system of power, Alikhanov has succeeded personally in smoothly navigating his own election as the oblast governor, ensuring Vladimir

Putin's good result in the presidential elections in March 2018 in the region, and the smooth organisation of the World Cup in June and July 2018 (including the timely completion of the sports facilities that were at risk of falling behind schedule). Furthermore, his failure to tackle the challenges of social policy and attract investors to the region is attributable not so much to the regional factor as to decisions taken at the federal level, including Russia's attachment to an ineffective economic model, a bad investment climate, a seriously underfinanced and inefficient social policy, and Moscow's aggressive foreign policy for which Russia has been punished with Western economic sanctions.

Presidential elections in March 2018

Vladimir Putin's official result in the Kaliningrad Oblast was almost identical to the Russian average (76.35% compared to 76.69% across the country) and much better than in 2012 when he won only 52.55% of the vote in the oblast (the second-worst result after Moscow where he won 47.72% of the vote) against the significantly higher national average (63.6%). The turnout in 2018 was slightly lower in the Kaliningrad Oblast than in the whole country (62.3% vs. 67.54%).²

Experts believe that Alikhanov's position is strong, compared to the other regional chiefs in Russia. This is also reflected in the rankings compiled by various institutions with more or less close links to the Kremlin. It is worth noting here that the rankings do not so much reflect any objective factors determining the robustness of a given governor's position, but rather the current balance of power in the ruling elite and the extent to which the given governor is useful for the Kremlin in the pursuit of its current objectives.

Alikhanov in governor rankings

In the Governors' Influence Ranking, prepared in January 2019 by the Kremlin-based Political and Economic Communication Agency APEK, Alikhanov ranked 15th among the 85 governors. According to the Minchenko Consulting expert group's ranking announced in September 2018, although Alikhanov's position has weakened, he still ranks high (second) in the ranking of the regional heads of the Northwestern Federal District

² 'После обработки всех протоколов в Калининградской области Путин получил 76,35% голосов', Калининград.Ру, 19.03.2018; 'Карта голосования: явка и результат Путина по регионам России', Ведомости, 18.03.2018.

(10th in the Russia-wide ranking), gaining seven out of ten points in the “Putin’s support” category, four out of five points in the “major project management” category and two out of three points in the “quality of political management” category. The ranking points out that there is a growing intra-regional conflict, which may indicate that the regional elite is becoming increasingly dissatisfied with Alikhanov. According to the Medialogia agency, which monitors and analyses media and social networks, in 2018 Alikhanov’s position significantly deteriorated in comparison to other governors (from 13th to 23rd position) and he did not make it to the top-20 regional heads most frequently mentioned in social networks. This is partly because he has been less active in the media than in 2017, the year of the gubernatorial elections in the Kaliningrad Oblast.³

It is unclear whether and to what extent corruption practices in the region have decreased due to Alikhanov’s actions – no specific information on this subject has yet emerged, although several anti-corruption investigations are underway in the region. One of them concerns embezzlement surrounding the construction of the stadium in Kaliningrad and a former construction minister in the government of former governor Nikolai Tsukanov has been arrested as part of it.⁴ Formally, the regional administration is fighting corruption. For example, in December 2018, as part of the implementation of Vladimir Putin’s national guidelines, Alikhanov established an anti-corruption service (tasked with ‘preventive’ activities). On 30th May 2018, at the request of Alikhanov, Kaliningrad City Council adopted an amendment to its statute allowing the governor to initiate the dismissal of councillors who violate anti-corruption laws. However, there are many indications **that pre-existing corruption schemes are merely being centralised and taken over by newly appointed persons linked to Moscow**, including representatives of the Alikhanov team, and that local elites have been deprived of part of their proceeds from corruption. This applies, among other things, to the municipal water supply company Vodokanal in Kaliningrad, previously under the control of Mayor Yaroshuk. The former director of the company, Alexander Ivashchenko, was dismissed

³ ‘Рейтинг влияния глав субъектов РФ. Российские регионы и региональная политика в декабре 2018 года’, АРЕК, 9.01.2019; ‘Алиханов теряет лидерские позиции в рейтинге устойчивости глав регионов’, RuGrad.EU, 30.09.2018; ‘В 2018 году Алиханов потерял 13 позиций в медиарейтинге губернаторов’, Новый Калининград, 29.01.2019.

⁴ Two businessmen, the Magomedov brothers, were arrested in 2018 in connection with this investigation, among others (the case then took on a federal dimension). For more information see: I. Wiśniewska, ‘The Magomedov brothers under arrest: growing rivalry inside the Russian elite’ [series: “OSW Analyses”], 11.04.2018.

in November 2018. He has been accused of embezzlement and an arrest warrant has been issued for him. There are plans to centralise water management in the whole region by transferring the ownership of the existing companies from the municipal authorities to the regional authorities. In June 2018, the regional parliament adopted a law on the matter.

According to independent media reports, during Alikhanov's term of office **the transparency of the decision-making process has been gradually eroding**. Meetings of the regional government, including meetings with representatives of municipal authorities, are increasingly often closed to the media, as are Alikhanov's meetings with business representatives. Against this background, it is worth noting that the governmental Corporation for the Development of the Kaliningrad Region has acquired, without a public offering, a 26% stake in the private regional radio and television station Kaskad. According to some commentators, the intention of the regional authorities is to create a governmental media holding company.⁵

2. Political opposition and repression

The political opposition in the region is weak and divided, just as it is in Russia generally. Representative government structures are dominated by the 'party of power', United Russia (UR). In the 2016 elections to the regional parliament and city council of Kaliningrad, UR won 29 seats out of 40 in the regional parliament and 20 seats out of 28 in the city council. The parties of the so-called licensed opposition and two deputies from the Patriots of Russia party (which is a *de facto* pro-Kremlin formation) also entered the regional parliament.

The activities of the 'licensed' parliamentary opposition, such as Genady Zyuganov's Communist Party of the Russian Federation, or Vladimir Zhirinovskiy's Liberal Democratic Party of Russia, **serve the interests of the government. The fragile anti-system opposition** is centred around the staff of Alexei Navalny, the Open Russia movement of Mikhail Khodorkovsky, and parties not represented in the parliament, such as Yabloko and Parnas. However, none of them plays a significant role and they regularly face repression (especially activists from Navalny's team and Open Russia). The weakness of the opposition does not stop the secret services from escalating their narrative

⁵ 'Расширение «закрытой части»: как правительство Алиханова прячет свою работу', Новый Калининград, 30.01.2019; 'Алиханов отказался объяснять покупку доли в телеканале «Каскад»', RuGrad.EU, 10.02.2019.

about a threat to the stability and security of the Kaliningrad Oblast posed by foreign agents and a local 'fifth column' – in line with the political strategy adopted at the federal level.

Despite the region's specific geopolitical situation and the special services' 'besieged fortress' narrative, the level of repression in the Kaliningrad Oblast does not differ from the Russian average. As in most regions, the authorities try to find the right balance between using repression for 'preventive' purposes (excessive 'liberalism' in this regard would be seen as a sign of the inability of both the secret services and the civilian authorities to control the situation in the region) and in order to reduce the scale of repression to what is deemed necessary – for image reasons and for fear of an uncontrolled increase in social discontent in the region. This is probably explained by the fact that **the authorities prefer to be cautious: they do not wish to excessively antagonise the local population**, which has proven itself capable of mass protest in the past. **Repression is thus applied selectively**, although in many cases it is painful. It mainly targets active supporters of Alexei Navalny and activists of Mikhail Khodorkovsky's Open Russia (OR). This is usually in connection with their activities driven by the general dynamics of social protests in Russia. The detentions and administrative penalties for coordinators of Navalny's staff in October 2018 in connection with environmental protests or pension reform protests may serve as an example of this. In addition, in December 2017 and on other occasions, OR activists have been held administratively liable for working with an "undesirable organisation".

In April 2018, the independent newspaper *Novye kolyosa* suspended the publication of its paper version due to significant difficulties in distribution. Its editor-in-chief Igor Rudnikov was kept in custody since November 2017 until June 2019 on charges of attempting to force a bribe from the regional head of the Investigation Committee. The case was unclear because, apart from the fact that Rudnikov may have disturbed the authorities with his journalistic and investigative activities, it is possible that he may have been a victim of, or used as a tool in, rivalry between the local services. This may indirectly be confirmed by the fact that the Rudnikov trial was not only taking place outside the Kaliningrad region (in St. Petersburg), but was also classified as secret. In June 2019 Rudnikov was acquitted and released – the move was most probably motivated by the angry social reaction to the repression against another journalist, Ivan Golunov.⁶

⁶ See: J. Rogoża, 'Rosja: sprawa Gołunowa i sukces presji społecznej' [series: "OSW Analyses"], 12.06.2019.

The most famous case of political repression in recent years has been the **criminal case brought against the fringe nationalist-monarchist organisation BARS (Baltic Vanguard of the Russian Resistance)**. In recent years, the organisation has vexed the authorities, including in connection with its criticism of the war launched by Russia in Ukraine. However, it in no way posed a political threat because of its insignificant clout and low recognisability. Its three activists, arrested in May 2017, were initially accused of extremism (a crime is punishable by up to ten years' imprisonment), including efforts to forcefully seize power in the Kaliningrad region and wrest the oblast away from Russia for it to join the EU. In October 2018, the prosecution changed the classification of the alleged acts to terrorism (organisation of a terrorist group), punishable by life imprisonment for the leader of the group, Alexander Orshulevich. The case will be heard by a military court in Moscow. The human rights organisation Memorial considers the detainees to be political prisoners.

The BARS case is part of **the secret services' and law enforcement agencies' fight against alleged extremism**, which has been noticeably stepped up in recent years (but which generally serves mainly to boost crime detection statistics and stifle freedom of speech). This case has also been used in the 'anti-Germanisation' campaign (the BARS leader called for the restoration of the name Königsberg to Kaliningrad) and served as a pretext for the attack on the German-Russian House in Kaliningrad (see below), as well as for broader repressions against activists of the Kaliningrad staff of Alexei Navalny and Open Russia. Among other instances, in August 2017, a search was carried out on OR activists (and Navalny's team members) as Open Russia was accused of financing BARS as its militant wing.

In February 2019 Kaliningrad saw Russia's first administrative case initiated under the law on punishment for the participation of minors in unsanctioned protest actions (the law was adopted in December 2018; the unsanctioned action in this case was a protest on 7 February against the use of torture against Alexander Orshulevich). The organiser of the protest, Ivan Luzin (an activist of Navalny's staff) was fined 30,000 roubles (ca. US\$ 460).

3. Public sentiments and social activity

Social moods in the region are to a large extent conditioned by the social and economic situation and problems occurring in this sphere. **The standard of living in the region is below the Russian average.** Residents are dissatisfied with the increase in prices and municipal tariffs, the raising of the retirement

age and environmental problems. However, this dissatisfaction manifests itself mainly in online discussions and, in individual cases, in open letters addressed to the regional authorities by groups of activists.⁷ It translates into active street protests only to a small extent. The level of social activity, including protest activity, in the Kaliningrad region shows a negative dynamic compared to the previous decade. According to the report of the Institute of Regional Expertise⁸ in 2019 the Kaliningrad Oblast ranks 23rd among the Russian regions in terms of protest activity; it has been classified as a region with a visible (but not 'high') level of activity. The protests taking place are often co-organised by the regional branches of political parties – both opposition parties and parties closer to the authorities (except for United Russia).

The raising of the retirement age in 2018 was the biggest factor in spurring social discontent in the Kaliningrad Oblast. The issue has led to considerable social resistance throughout Russia. According to polls, more than 90% of respondents are against this measure. In the Kaliningrad region it particularly affects men whose average life expectancy, according to Rosstat's Kaliningrad branch, is 67 years (i.e. only two years above the new retirement age). The protest against the reform in July 2018 was around 1,000-strong in Kaliningrad, and the demonstrators chanted not only social slogans but also political ones, such as "Putin, retire, Medvedev, resign".⁹ Other examples of protests included actions against pollution (including landfill sites), fuel price rises, and the arrest of a local investigative journalist and former member of the regional parliament Igor Rudnikov. The protests usually attracted people in the dozens.

The attitude towards the regional leader, Governor Anton Alikhanov, a politician from outside the region who represents the interests of Moscow, is one of moderate optimism and passive acceptance.¹⁰ In the gubernatorial elections

⁷ С. Шерстюк, 'Открытое письмо Губернатору Калининградской области Алиханову А.А.', RuGrad.EU, 26.03.2018.

⁸ Рейтинг протестной активности российских регионов, Институт региональной Экспертизы, February 2019.

⁹ Ю. Парамонова, 'На митинге оппозиции в Калининграде потребовали отправить Путина на пенсию', RuGrad.EU, 31.07.2018.

¹⁰ There are no current surveys on public support for Alikhanov. In the October 2016 survey conducted after his nomination was announced, 54.3% of respondents hoped for change for the better, 32.3% said they did not expect anything good, and 13% had no opinion. When asked whether the appointment of the young governor opened up new prospects for the region, 43.5% answered in the affirmative, 36.7% said the opposite. See: 'Опрос: Боле половины жителей Калининграда ждут лучшей жизни при Алиханове', Калининград.Ru, 12.10.2016.

Alikhanov won 81% of the vote. **The governor is not supported by the regional intellectual elites**, who accuse him of misunderstanding the specificity of the region, **but the majority of the inhabitants seem to passively accept his policy**. This contrasts with the active expressions of discontent towards the previous governor from outside the region, Georgy Boos. Protests against him in 2010, up to 10,000-strong, eventually led to his resignation.

Although protest activity in the region is currently relatively low, **there are many grassroots social initiatives**, mostly apolitical, related to the protection of the cultural heritage of the region or charity work. There are many social groups and associations such as “The Right to the City”, bringing together local activists dealing with various aspects of urban life – ecological, social, municipal, architectural, etc. They campaign for the revitalisation of neglected urban spaces with historic buildings (fortifications, etc.).¹¹ Because of the difficult environmental situation of the region – water contaminated by sewage, problems caused by landfills (activists are still discovering new illegal landfills despite the declaration of the authorities to eliminate all of them in 2016), tree felling in cities – environmental organisations are active in Kaliningrad, including Ekozashchita or regional branches of the Green Front organisation. They organise pickets, blockades of trees scheduled to be felled, social campaigns to clean up the coastline, etc. Many initiatives are created and developed on the Internet, in thematic groups such as Musora.bolshe.net, which conducts educational campaigns on waste sorting, or the Avenues of Kaliningrad Oblast, which maintains the tradition of caring for old trees and publicises felling plans.

In 2018, Kaliningrad hosted the “City of Rights” human rights festival for the first time. This festival brings together human rights activists, urban planning and urban ecosystem activists, charities, and people interested in culture and social art. Kaliningrad activists are inspired by the Polish social campaign “Living Street”, which involves the transformation of neglected public spaces. In Kaliningrad there are a number of places that combine the functions of public spaces, museums, conference rooms, coworking spaces and restaurants and attract activist communities, e.g. the art-space “Gate” located within the historical walls of the Sackheim Gate, which further underlines the interest of activists in the pre-war roots of the region.

¹¹ See: А. Колотыгина, К. Черёмушкина, ‘Вал проблем: Попытки «оживить» Литовский вал и их результаты’, Твой Бро.

For six years now, the Kafka and Orwell Forum – an independent discussion forum, supported by local business and the Civil Initiatives Committee of former Deputy Prime Minister Alexei Kudrin – has been held in the Kaliningrad part of the Curonian Spit. Invitees include opposition politicians, experts, columnists and poets including Lew Shlosberg, Yevgeny Roizman and Andrey Orlov. The forum has been the subject of the attention of the regional authorities from the beginning. During the last meeting in September 2018 the OMON special forces carried out a raid in the hotel where the participants stayed, accusing them of drug trafficking.¹²

The World Cup 2018, which included some matches held in Kaliningrad, **was an opportunity to open the region up to the world and intensify people-to-people contacts between the region's inhabitants and foreign tourists.** During the World Cup, the region was visited by 260,000 thousand tourists, including 90,000 foreigners.¹³ The plans to build a cultural and entertainment complex in Kaliningrad on the island of Oktyabrsky, where the new stadium is located, may attract even more visitors to the Kaliningrad Oblast, both foreign tourists and those from other regions of Russia. A branch of the Tretyakov Gallery, an opera and ballet theatre, and universities are to be based there (the completion of the complex is scheduled for 2023).¹⁴

4. Regional identity and the so-called Germanisation problem

The social and historical identity of the inhabitants of the Kaliningrad Oblast remains complex, but it includes a strong identification with the region and with Europe. The highest result (50%) was of residents who identify primarily as 'Kaliningrad people', i.e. inhabitants of Kaliningrad and the Kaliningrad Oblast), a slightly lower percentage identify as 'Russians, citizens of Russia' (44%), while 3% identify as 'Europeans (those and the following figures are based on a KMG poll in October 2018¹⁵). Those who see themselves as 'citizens of Russia' are more likely to be people who have moved to Kaliningrad from mainland Russia or from the CIS area relatively recently. When

¹² О. Зурман, В. Невар, 'Кафка, Оруэлл и силовики: что произошло после форума в Светлогорске', *Новый Калининград*, 18.09.2018.

¹³ *Ростуризм подвел туристические итоги Чемпионата мира по футболу FIFA 2018 в России*, Federal Tourism Agency, 3.08.2018.

¹⁴ 'Путину показали, как будет выглядеть культурный комплекс на Острове в Калининграде', *Калининград.Ru*, 8.01.2019.

¹⁵ *О Калининградцах – Опрос жителей города Калининграда (октябрь 2018)*, Исследовательская компания «КМГ», 16.11.2018.

describing themselves, the inhabitants of Kaliningrad most often selected the following descriptions: 'people with a European mentality and lifestyle' (22%), 'friendly, open and hospitable people' (13%), 'people whose lifestyle is different than elsewhere in Russia' (4%), but also 'abandoned people' and 'not needed by anyone' (3%).

The people of Kaliningrad admit to being distinct from the rest of Russia – 96% believe that their region is different from other Russian regions. In an open question about the region's distinctive characteristics, 50% pointed to amber extraction, 50% to the region's location on the Baltic Sea, 42% to neighbourhood of the European Union, 34% to the unique history, 22% to the separation from the rest of Russia, and 21% to the unique nature. **The perceptions of the positive and negative aspects of the region's location were distributed evenly:** 15% of respondents believe that the oblast's location generates more opportunities, 16% think it generates more problems, 40% think there are as many opportunities as problems, and 23% say it does not affect their lives in any way.

References to the region's pre-war history may not be dominant in the regional identity but they form an important part of it. When describing the region's capital city, the inhabitants chose phrases such as 'a city with a history' (11%) or 'little Europe' (9%), and some even said 'Russian Europe' or 'Russian Germany'. Most respondents (53%) unequivocally considered the Protestant cathedral where Immanuel Kant is buried to be the most important historic monument of Kaliningrad. **The residents of Kaliningrad did not share the concerns, sometimes raised by the government, about the increased cultural influence of Germany** or attempts at imposing German culture and tradition on them. The phenomenon was observed, in varying degrees, by 9% of respondents, while 86% said they did not experience it. The percentage of the region's residents who are in favour of restoring Kaliningrad's pre-war name of Königsberg is also small, but not marginal at 12%, while 81% of residents are in favour of maintaining the current name. Thus, there is rather a kind of snobbery about 'Germanness', which is treated not so much as an identity point of reference, but rather as a kind of folklore, as well as a synonym for quality and a tourist brand.

This persistent sense the oblast's residents have of being distinct has been influencing Moscow's perception of the political and economic situation in the Kaliningrad Oblast. Because of its geopolitical importance, the region has been the object of specific ideological and propaganda efforts,

including in the field of historical policy. There is no unanimity among the decision-makers involved on the detailed content of this policy.

The alleged ‘Germanisation’ and the need to counter it (i.e. the memory of the German heritage in every dimension) **are permanent topics in the regional public debate about identity and history**, artificially stoked by the ‘patriotic communities’ gathered around several pro-Kremlin media outlets with limited reach in the region (including the Regnum agency), and promoted and exploited by the army and the special services. **At the official level there is a clear tendency to obliterate or ignore the German heritage** (perhaps with the exception of Immanuel Kant and his legacy), despite the pretence of actions aimed at e.g. protecting German architecture.

Before 2016, there was relatively little discussion about ‘Germanisation’ and most of it was connected with the repeated initiatives to rename Kaliningrad as Königsberg, while the criticism was limited to several ‘patriotic’ media outlets. **The anti-Germanisers became much more active in the spring of 2016**, when **Nikolai Dolgachov** became the chief of the regional branch of the All-Russian State Television and Radio Broadcasting Company (VGTRK, the largest state-owned media holding). Together with **Andrey Vypolzov** of the Regnum agency, Dolgachov unleashed a defamation campaign against the alleged ‘Germanisers’ (the ‘fifth column’). Among those targeted by the action were: the Kaliningrad-based cultural institution German-Russian House (GRH) (the only one of its kind in Russia that was not subject to the official structures of the German minority in the Russian Federation), and representatives of the intelligentsia and the opposition calling for the protection of German historic monuments in the region.

The regional branch of the VGTRK broadcast a number of anti-German and anti-opposition programmes. In August 2018, it broadcast a programme discrediting the non-governmental organisation Zelenogradsk-Pinneberg which had been working with German partners within the framework of a partnership between the two cities of the organisation’s name since the beginning of the 1990s. The youth exchange trips to Germany that it organised were presented as recruitment activities for the German special services. After attempts were made to assign the organisation the status of a ‘foreign agent’ it dissolved its official structures in March 2016, although it continues to work on an informal basis.

There are many indications that the intensification of the “anti-Germanisation” media campaign was a personal initiative of Dolgachov and

Vypolzov but which was however supported by the secret services and was in line with their strategy in the Kaliningrad Oblast and the political interests of the Kremlin. Already in March 2016, i.e. before Dolgachov's arrival in Kaliningrad, a branch of the Academy of Geopolitical Problems (affiliated with the Ministry of Defence) was opened in this city, promoting the narrative of a "powerful information war in the region", in which Germany was allegedly carrying out activities to eradicate Russian identity. In the fight against "Germanisation" the BARS case was used instrumentally. One of the things which this led to was the final crackdown on the German-Russian House (GRH), closed in 2017 (there are many indications that BARS allowed itself to be used as a tool in a provocation against the management of the GRH).

The case of the GRH is a clear indication of **the real objectives of the Russian authorities and services. They aim not only at 'protecting Russian identity' against the attempts of 'Germanisers' – they also seek to appropriate the concept of 'Germanness' in order to further Russian political, economic and secret service interests.** Shortly after the closure of the GRH in October 2017, it was reopened as an entity subordinated to the official structures of the Federal National and Cultural Autonomy of Russian Germans, led by Genrikh Martens, who in the past was active (as a trustee) in Vladimir Putin's election campaigns. Martens has openly spoken out against the "Germanisation" of the Kaliningrad Oblast, pointing to the "Russianness" of ethnic Germans living in Russia. The mission of the new GRH has been extended. Apart from cultural activities it is now tasked with promoting economic and business contacts between Russian and German entrepreneurs.

Occasionally, the 'opponents of Germanisation' commit acts of hooliganism in the Kaliningrad Oblast. One example of this was in November 2018 when the Kant monument in Kaliningrad, his tombstone and memorial plaque were defaced (covered with paint). Leaflets were scattered around, calling Kant a traitor, an enemy and a German. Provocations targeting Russian memorial sites have also taken place whereby the supposed 'Germanisers' placed Nazi symbols or calls to overthrow the Russian government on defaced monuments.

The aggressive 'anti-Germanisation' efforts, consistent with the Kremlin-promoted image of Russia as a 'besieged fortress', do not necessarily fit in with the interests of the regional authorities who care about good relations with Germany and strive to improve the investment climate in the region and strengthen its image as an attractive tourist destination. The anti-German media campaign has also been criticised by the regional representation of the

Ministry of Foreign Affairs of the Russian Federation,¹⁶ which has been actively lobbying for Russian geopolitical and business interests in Germany. **The official positions of the Kaliningrad authorities**, including Alikhanov and Tsukanov before him, **prove they wish to distance themselves from this kind of propaganda campaign** (Alikhanov said in 2016 that the issue of the Kaliningrad Oblast's Germanisation was 'made up'), although they have not been actively countering this kind of initiative. **The position of the authorities on the demands for better protection of Kaliningrad's post-German historical heritage is also ambiguous. Most likely it is influenced by specific business interest of groups with links to the region's authorities.** Governor Alikhanov has stopped all speculation about the possibility of rebuilding the medieval Royal Castle in Kaliningrad, opting instead for the completion of the long decaying House of Soviets, built on the ruins of the castle in Soviet times. However, he has declared (already in November 2016) his willingness to rebuild the old German railway stations (so far the station in Pionersky has been renovated), and in February 2018 an action plan to compile an inventory of historical heritage sites was announced. A debate is also going on (mainly at the civil society level) on the future of German post-industrial buildings in which supporters of a demolition that would free up attractive plots for development clash with advocates of renovating these zones and incorporating them into the tourist and recreational urban space.

¹⁶ 'Региональное представительство МИД РФ опубликовало заявление в защиту немецких НКО', RuGrad.EU, 2.06.2016.

II. ECONOMIC SITUATION AND POLICY IN THE KALININGRAD OBLAST

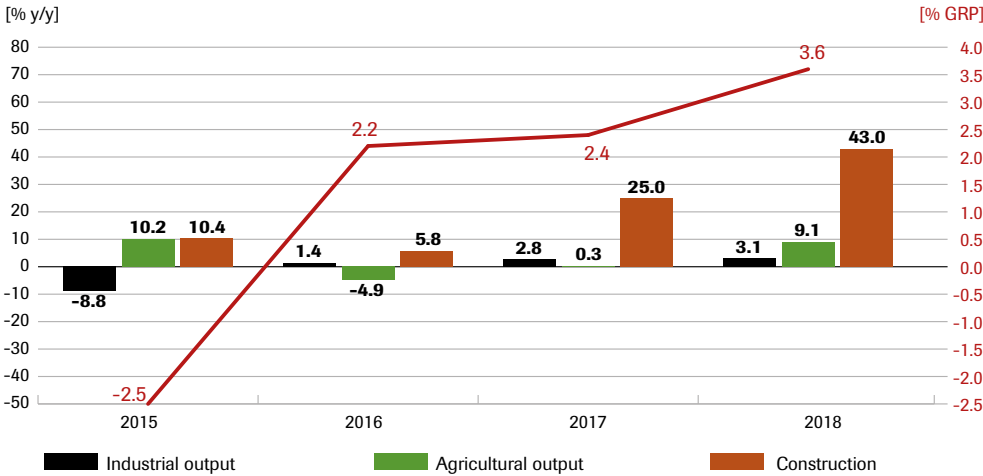
1. Social and economic situation

The economic situation in the Kaliningrad Oblast is closely dependent on the development of the situation in the whole of Russia. **After the collapse of 2015, the oblast's economy has been growing for the last three years, and the region's growth rate as well as most of the macroeconomic indicators have been much better than the Russian average.**¹⁷ Several factors contributed to this, including in particular the influx of federal funds to the region (significant compared the oblast's size) for infrastructure projects, including the construction of a floating LNG terminal on the Baltic coast, the expansion of the energy infrastructure, the construction of a football stadium and the expansion of an airport which was necessary for the organisation of the 2018 FIFA World Cup matches. However, it should be noted that some of the federal investments, which had a positive impact on the region's economy during their implementation (by providing employment and contracts for local companies), in the long run will not become a driver of revenue growth for the Kaliningrad Oblast. They may even turn out to be a burden for the region. In the case of the LNG terminal, the investment has increased the energy security of the Kaliningrad Oblast, but it is doubtful whether the terminal will be used. If it is, the gas supply via this route will generate significant costs for Gazprom (for more information see Chapter II.2.2) and the federal budget. The situation with the football stadium, whose costs of 70 million a year will be shouldered by the regional budget as of 2022, may prove much more difficult from the perspective of regional finances.

It should be noted that the federal authorities are trying to maintain a high level of federal funding flowing into to the region, which is likely to have a positive impact on the regional economy in the years to come. There are plans to build a cultural centre in Kaliningrad, which will cost twice as much as the football stadium, and the road network in the region and regional ports are being expanded and modernised.

¹⁷ Macroeconomic indicators are quoted from [Rosstat](#) (the statistical office of the Russian Federation), and [Rosstat, Kaliningrad office](#).

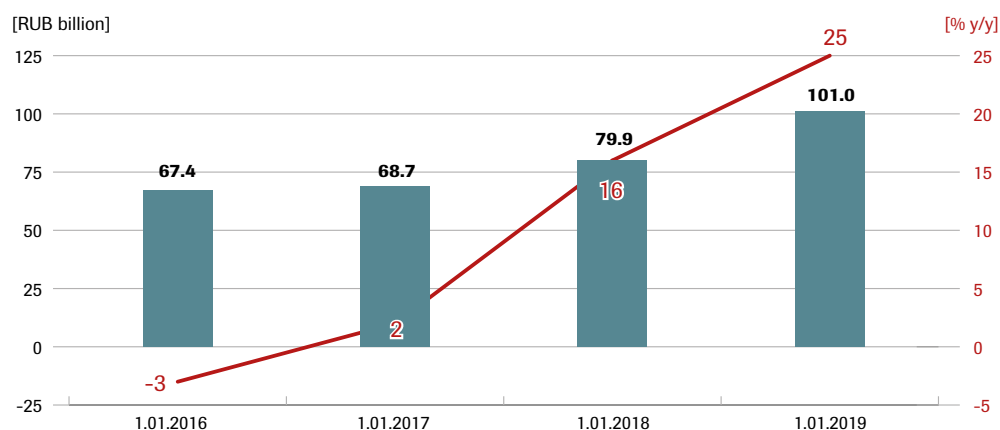
Chart 1. Gross regional product of Kaliningrad Oblast and industrial output, agricultural output and construction



Source: Rosstat

In addition, the availability of bank loans has had a positive impact on the economic situation of the region in the last two years, reflecting the attractiveness of interest rates due to low inflation and lenient bank lending requirements. In a situation of falling real incomes, Kaliningrad residents maintained consumer demand by taking out bank loans (in 2018 the volume of private debt in the region increased by about 25%, see Chart 2), which contributed in particular to the increase in sales on the automotive and mortgage markets. As a result, the Avtotor plant located in the Kaliningrad Oblast – one of the largest car manufacturers in Russia and the largest manufacturing company in the region (accounting for around 50% of the oblast’s manufacturing industry) – has recorded a dynamic increase in production in the last two years (more than 50% in 2017 and around 40% in 2018, with sales increasing by 12% and 13%, respectively, in those years). Avtotor’s results have improved also due to the state financial support the company has been receiving from the federal budget since 2016 as compensation for the abolition of the customs privileges it benefited from before the changes in the functioning of the Kaliningrad Special Economic Zone (see below). However, maintaining domestic demand at its current level due to loans will be very difficult. On the one hand, rising inflation has been associated with rising loan interest rate prices, and on the other, the central bank, concerned about the excessive indebtedness of the population, has taken steps leading to a tightening of banks’ credit policies.

Chart 2. Personal debt levels in the Kaliningrad Oblast (in billions of roubles, as of first day of year and annual change in %)



Source: Central Bank of Russia

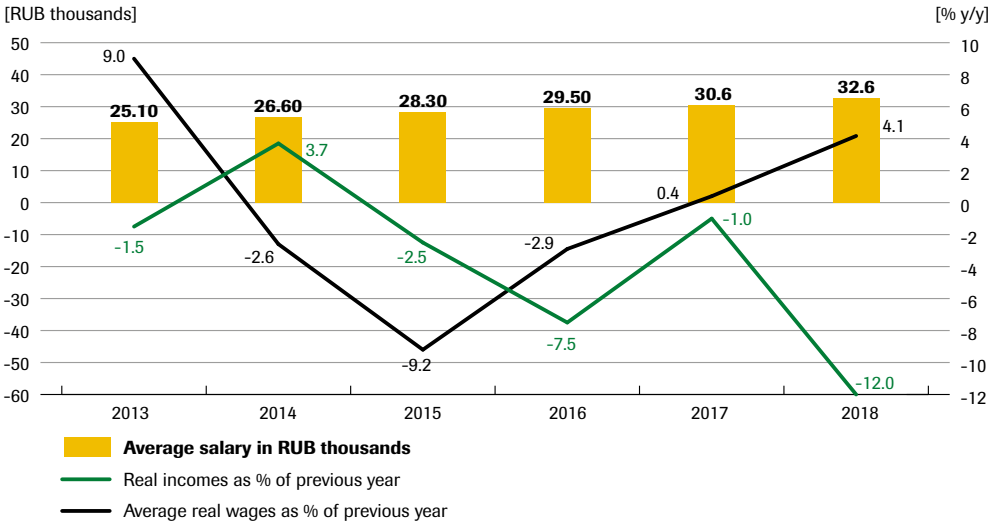
In 2018, **agricultural production in the Kaliningrad Oblast increased as well (by 9%)**. Several factors contributed to the growth of companies in this sector, in particular protection against foreign competition (provided by protectionist state policy and counter-sanctions), preferential bank loans (below the rate of inflation), and, above all, extensive preferences available within the Special Economic Zone.

Inflation in the region in 2018 grew at a higher rate (4.8%) than the average for Russia (4.3%), with prices of industrial goods increasing by 5.3%, and food prices by 4.6%. The increase in the prices of some goods, especially foods, was much higher than the general inflation rate. For example, the price of eggs in the oblast rose by over 35% in 2018, and the price of petrol increased by almost 10% (despite state intervention).

Despite positive macroeconomic trends, the **standard of living in the Kaliningrad Oblast remains below the Russian average** – the region ranks 44th in the socio-economic ranking of Russian regions (out of 85 regions). The gross regional product *per capita* in the Kaliningrad Oblast is about 80% of the Russian average. People's standard of living in the Kaliningrad Oblast, like in the other regions, has not improved after the slump in 2014–2016. Although real wages have been rising in the region since 2017 and increased by 4% in 2018, real incomes have been constantly declining for five years. Unemployment in the region has been steadily falling and in 2018 stood at 4.7%, which places Kaliningrad in 32nd position among all regions of Russia.

The Kaliningrad Oblast is one of the few regions in Russia that recorded a population growth in 2018. The total number of inhabitants of the region has exceeded one million. However, the reason was not so much natural demographic growth as a positive migration balance. Rosstat figures show that on 1 January 2019, 1,002,271 people lived in the Oblast – that is 7,672 more than the year before. Although the birth rate was negative (10,316 people were born and 12,111 died), this was compensated for by a positive migration balance: 47,266 people came to the region and 37,799 people left. The majority of the immigrants came from other regions of the Russian Federation, while the main foreign countries of origin included Kazakhstan, Kyrgyzstan, Uzbekistan and Ukraine.¹⁸

Chart 3. Real incomes in the Kaliningrad Oblast



Source: Rosstat

¹⁸ Официальная статистика – Население, Калининградстат.

2. The Kaliningrad Oblast in the economic policy of Moscow

In the last few years Moscow's policy towards Kaliningrad Oblast has become increasingly coherent and consistent. The Kremlin is visibly interested in the region and shows the political will to engage with it, which has resulted in an increase in federal spending in the region.

On the one hand, Moscow's growing interest in the Kaliningrad region is an element of the Kremlin's regional policy being implemented throughout the country, which aims to increase the centre's control, including economic control, over the regions, while at the same time tightening the system of public finances by reducing corruption-generating mechanisms and increasing the effectiveness of public spending. However, due to Western sanctions and limited opportunities to earn income abroad, public investment has become a source of financing and a way to expand personal wealth for many oligarchs in President Putin's inner circle in recent years. As a result of Moscow's policy, the Kaliningrad Oblast has seen the growing presence and importance of federal-level corporations such as the state-owned corporation Rostec, Gazprom, Russian Railways and companies controlled by Putin's friends Arkady Rotenberg (Stroygazmontazh) and Gennady Timchenko (Stroytransgaz).

It is a permanent feature of the Kremlin's policy towards the Kaliningrad Oblast that it strives to find a balance between, on the one hand, isolating the region from its European and NATO neighbours and using it as a foreign policy instrument, and on the other, taking advantage of its special location to derive economic benefits for the region and Russia from cooperation with its neighbours.

The growing activity of the Kremlin in the Kaliningrad Oblast and Moscow's efficacy in pursuing its main policy objectives have manifested themselves in the last few years in the implementation of several major investment projects, including the development of the region's electricity and transport infrastructures and the organisation of matches of the 2018 FIFA World Cup, as well as in the new rules for the special economic zone and the creation of a 'tax haven' for foreign-registered companies moving their operations to the region.

The most important measures taken by Moscow with regards to the region included:

2.1. New rules for the functioning of the Special Economic Zone

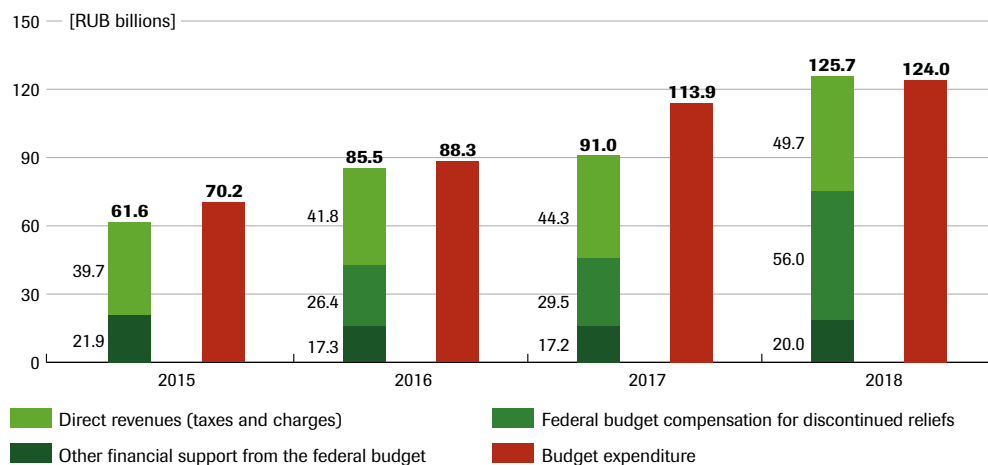
Due to its unique geographical location, since the beginning of the 1990s the region has been operating on special economic principles aimed at overcoming barriers hindering its economic development, related to transport problems, a small internal market and the dependence on imports. The rules for the functioning of the **Special Economic Zone (SEZ)**, laid down in federal laws,¹⁹ have been change on several occasions during the last twenty years. The changes introduced since 2006 have been aimed, on the one hand, at reducing the losses incurred by the Russian budget as a result of customs exemptions for entities registered in the zone (initially, several thousand businesses were eligible). On the other hand, they have been a way of limiting the number of entities to which exemptions were granted, and thus centralising the regional economy by promoting large, mostly federal, enterprises. This was the purpose behind the introduction, in 2006, of a high minimum investment threshold of RUB 150 million for residents (around US\$ 5 billion based on 2006 exchange rates). However, as the Kremlin gradually abolished the customs duty reductions for Kaliningrad residents in a process which was eventually completed in 2016, the federal authorities tried to prevent a decline of the local economy and made the SEZ more attractive also to smaller investors. In particular, since 2016 the federal budget has provided the region with special funds: in 2018 it was 55 billion roubles (approximately US\$ 0.8 billion) to compensate businesses for the abolition of tariffs privileges. The compensation measures resulted in a significant increase in the level of federal financial support for the region and thus its financial dependence on the Kremlin. As a result, in 2017 Kaliningrad Oblast joined the narrow group of eight Russian regions in which federal financial assistance accounts for more than 60% of all budget revenues, while back in 2015 it this figure had been only 30%.²⁰ As it turned out, though, only a few residents of the zone benefited from the state support, and its main beneficiary was the automobile corporation Avtotor, which cashed in 80% of all the funds.²¹

¹⁹ See: [Администрация Особой экономической зоны в Калининградской области 2019](#).

²⁰ See: [Министерство финансов Калининградской области 2019](#).

²¹ No information is available on the amount of compensation payments to Avtotor in 2018, although it probably remained at a similar level as in 2016 and 2017.

Chart 4. Kaliningrad Oblast's budget revenues and expenditures



Source: Ministry of Finance of the Kaliningrad Oblast

The **changes introduced on 1 January 2018** were of particular importance for the region's economy and concerned, among others, extending the application of preferential rules until 2045 (by 14.5 years) and expanding the area of the SEZ to include sea port areas, as well as reducing the minimum investment threshold to 10 million roubles (US\$ 150,000) for health care investments and to 1 million roubles (US\$ 15,000) for IT projects. Moreover, SEZ residents can pay reduced social security premiums and a zero income tax rate for six years after the first year with a recorded profit, and in the next six years they can pay half of the regular rate (previously similar preferences were available for six years from the granting of resident status). In addition, a zero VAT rate was introduced for the carriage of passengers and luggage by air (previously 10% VAT). However, the of electronic business, tourist and humanitarian visas introduced in July 2019 will be of key importance for boosting Kaliningrad's co-operation with other countries and for attracting foreign investors and tourists (for more information see Chapter III.2).

Changes introduced in 2018 to the rules of how the SEZ functions mean that the number of entities registered as resident there has increased by 70 (i.e. by 30%), and some 30% of the newly registered businesses were IT sector companies. The second-largest group of new businesses comprised agricultural and foodstuff companies.²² In 2018, Kate-Development, an automotive gearbox manufacturer owned by Yekaterina Ignatova, also became registered in the zone. Kate-Devel-

²² Администрация Особой экономической зоны, *op. cit.*

opment works very closely with the state-owned corporation Rostec controlled by Yekaterina's husband Sergei Chemezov, one of President Putin's close friends. It should be added that since taking over the Kaliningrad Amber Combine in 2012, Rostec itself has also been present in the Kaliningrad Oblast.

Less than 300 businesses currently have their headquarters registered in the SEZ. At the beginning of 2016 approximately 800 businesses in the region benefited from the reduced tariffs (available within the SEZ from 1996).

Avtotor

The joint-stock company Avtotor is one of the largest manufacturers of foreign car brands in Russia. Its plants currently assemble cars for BMW, Hyundai, KIA, TATA Daewoo and FAW. The company recorded a peak volume of production in 2012 when it manufactured 265,000 vehicles. Since the slump in 2015 when its output decreased to around 90,000 cars, the company has been increasing its production volume. In 2017, the company recorded growth of over 50% and, according to preliminary data, its production increased by a further 40% in 2018 – to approximately 203,000 cars and trucks. Avtotor sales increased by 12% and 13% respectively in this period.

Avtotor is the cornerstone of the Kaliningrad Oblast's economy, accounting for:

- around 50% of the Kaliningrad Oblast's manufacturing sector;
- 57% of the region's maritime and rail container shipments;
- 39% of taxes paid in the Kaliningrad Oblast.

However, of the approximately 67 billion roubles of taxes paid in 2018, only approximately 1 billion roubles were allocated to the regional budget. The company could receive about 45 billion roubles (about US\$ 0.8 billion) in compensation from the federal budget for the abolition of reduced tariffs in 2018.

It is not clear who the real owner of the corporation is. In the early 1990s, Vladimir Shcherbakov founded Avtotor (originally as a KIA assembly plant in the Kaliningrad Oblast) and according to media reports, he controlled about 99.9% of the company. During the years of the Soviet Union, Shcherbakov worked as an engineer and then as a director in the VAZ and Kamaz car factories, then pursued a political career in Moscow and in 1991 became the First Deputy Prime Minister and Minister for Economy

and Forecasting of the USSR (previously this department was called the State Committee for Economic Planning of the USSR). According to media reports, in 2016 Shcherbakov transferred his shares to his son Sergei, who lives in Switzerland. Sergei controls Avtotor through the Automotive Development Holding, registered in 2016 in Luxembourg and wholly owned by the Automotive Development Group Limited, registered in Hong Kong, also in 2016.

Considering that the Shcherbakov family does not belong to the core of the current Russian political and business elite, that it controls the plant through tax havens (at a time when President Putin is forcing Russian business to repatriate capital) and receives multi-billion-dollar compensation from the state budget, it may be assumed that the real beneficiaries of the company are not the Shcherbakov family, but people from Putin's inner circle.

2.2. Development of the potential of the energy sector

The measures taken by the federal authorities in the energy sector, mainly in the gas and electricity sectors, are also part of the strategy to further isolate the Kaliningrad Oblast.

The launch of the “Marshal Vasilevsky” floating LNG regasification terminal in January 2019 was a key investment in ensuring the gas self-sufficiency of the region.

The floating LNG regasification terminal in the Kaliningrad Oblast

The regasification capacity of the floating LNG regasification terminal is 2.3 million tonnes (approximately 3.1 billion m³) and the storage capacity is 174,000 m³. The unit was manufactured at the Korean shipyard Hyundai Heavy Industries in early January 2017, but due to damage to one of the regasification boilers it was handed over to Gazprom with an almost one-year delay, on 31 October 2018. Delays were also caused by the damage to the coastal infrastructure due to the storm in the Baltic Sea in November 2017. The project also required the construction of the appropriate offshore infrastructure, i.e. a 3.5 km long sea gas pipeline, leading from the terminal to the land part of the port and the offshore infrastructure (see Map 2). The eventual cost of constructing the floating unit was

US\$ 295 million (excluding VAT). The total budget including the costs of building the infrastructure in the Kaliningrad port (where Gennady Timchenko's Sroytransneftegaz was the contractor) amounted to RUB 60 billion (around 1 billion US\$).

The investment is part of the Russian strategy of strengthening the energy independence of the Kaliningrad Oblast. However, it is unlikely that the newly commissioned terminal will be fully utilised in the coming years.

The new infrastructure makes it possible for Gazprom to be able to avoid transferring gas to the oblast through a pipeline passing through Belarus and Lithuania, while fully satisfying the region's consumption needs (2.6 billion m³ in 2018). However, it is unlikely that in the coming years it will actually reduce gas transmission via the current transit route.

The chief reason for this is that Gazprom remains bound by a transit contract with Lithuania for the transmission of 2.5 billion m³ of gas annually till the end of 2025. In fact in October 2018 its representatives announced that in 2019, gas supplies to the region via Belarus and Lithuania would increase from 2.5 to 3.2 billion m³.

Secondly, the price of LNG imported to the Kaliningrad Oblast would be higher than the price of gas transmitted through the gas pipeline system (the price of gas supplied to consumers in the oblast currently amounts to approximately US\$ 70 per 1,000 m³, while LNG prices on the European market ranged between US\$ 200–300 per 1,000 m³ in 2018). In addition, Gazprom would not be able to supply its own LNG to the terminal. The gas liquefaction plant being built in the Leningrad region, near the Portovaya compressor station, is to be commissioned in the second half of 2019 and its production capacity is set to be only 1.2 million tonnes (approximately 1.6 billion m³),²³ which corresponds to only 61% of the oblast's consumption. Alternatively, supplies of LNG purchased by Gazprom on spot markets would generate very high costs. Thus it will be up to the Kremlin's political decision whether or not pipeline transit will be reduced in favour of LNG supplies.

²³ The contractor for the investment is OOO NIPI NG "Peton", and it will cost 127 billion roubles. Gazprom plans to sell gas from the LNG terminal in Leningrad Oblast to Finland and Estonia. 'Газпром создал подразделение, ответственное за подачу газа в Nord Stream 2', *Нефтегазовое обозрение*, 22–28 февраля 2018 года, pp. 37–38; 'Небольшие задержки. 1-й из 3-х комплексов СПГ в Ленинградской области запустят в феврале-марте 2019 г.', *Neftegaz.Ru*, 15.02.2019.

[illegible]

Meanwhile, the gas pipeline network in the region has been extended, which is an element of Gazprom's nationwide strategy for the expansion of gas networks in the Russian Federation.²⁴ In 2016, the 25 kilometre-long branch of the Minsk-Vilnius-Kaunas-Kaliningrad gas pipeline to Chernyakhovsk was put into operation. In October 2017, Gazprom completed the expansion of two branches of the pipeline – to Gusev and to Sovetsk. This increased the security of supply to the Mayakovskaya and Talakhovskaya thermal power plants²⁵ (see below). The gas network coverage in the Kaliningrad Oblast has increased from 54.5% in 2010 to 83.6% in 2018. This exceeds the national average (68.6%)²⁶. Alongside the development of the aforementioned branches, Gazprom opened three automatic gas distribution stations – in Chernyakhovsk in August 2016, and in Sovetsk and Gusev in 2017. In addition, Kryogaz, a company controlled by Gazprombank, is building a small LNG production plant in Kaliningrad with an annual capacity of 150,000 tonnes, to be completed in 2019.

Gazprom has also been expanding its gas storage facilities in the Kaliningrad region.²⁷ In September 2013, the construction of the first two gas depots was completed. In December 2017 a further two were completed. Their total capacity is currently 174 million m³. Ultimately, meaning by 2025, Gazprom plans to increase their number to 14, and their total capacity to 800 million m³ (daily delivery capacity will amount to 12 million m³).

The development of infrastructure enabling the use of natural gas as a car fuel is also an important element of the efforts to strengthen the region's energy independence. Gazprom Gazomotornoye Topливо, a subsidiary of Gazprom, operates a small LNG and CNG plant in Kaliningrad with an annual capacity of 21,000 tonnes (it also includes a gas compression station with a production capacity of 6,000 m³ per day).²⁸ On 24 December 2013, Gazprom Gazomotornoye Topливо signed an agreement with the government of the Kaliningrad Oblast to promote the use of natural gas as automotive fuel. At the end of 2016, four mobile fuel stations were opened in the region – in Bagrationovsk,

²⁴ The gas network expansion programme is 41% financed by the Russian Federation's regions, 56% by Gazprom and 3% by federal funds allocated under targeted programmes.

²⁵ 'Поставки природного газа потребителям Калининградской области', Gazprom, 27.01.2019.

²⁶ 'Виктор Зубков: в Калининградской области есть все предпосылки для выхода на новый уровень использования природного газа на транспорте', Gazprom, 29.05.2019.

²⁷ The programme was initiated in 2009.

²⁸ 'Компания «Газпром газомоторное топливо» приобрела комплекс по производству СПГ и КПГ в Калининграде', Gasworld, 4.07.2014.

Chernyakhovsk, Kaliningrad and Sovetsk – offering LNG and CNG to individual customers. According to 2018 figures, they sold 2.2 million m³ of gas to customers (11 times more than in 2015).²⁹

As regards the electricity sector, notwithstanding the suspension of the Kaliningrad Nuclear Power Plant³⁰ project, **Moscow has been developing electricity infrastructure in the Kaliningrad Oblast.** Before March 2018, three thermal power plants were in operation in Kaliningrad Oblast: Kaliningrads-kaya-1 (22.5 MW), Kaliningrads-kaya-2 (875 MW) and Gusevskaya (15.5 MW), as well as three hydroelectric power plants of little significance (Pravdinskaya, Ozerskaya, Malaya Zaozyornaya). On 2 March 2018, two new gas-fired thermal power plants, Mayakovskaya (in Gusev) and Talakhovskaya (in Sovetsk), with a capacity of 156 MW each, were officially commissioned. On 6 March 2019, in the presence of Deputy Prime Minister Dmitry Kozak and Minister of Energy Alexander Novak, the Pregolskaya gas-fired thermal power plant in the Guryevsk region of Kaliningrad (with a capacity of 455.2 MW) was commissioned.³¹ The total capacity of all power plants operating in the region is currently approximately 1,667.2 MW, which represents approximately 200% of the maximum annual electricity demand in the oblast.

The Primorskaya coal-fired power plant (with a capacity of 195 MW) is under construction – it is scheduled to be commissioned in the first half of 2020. The cost of construction of the four facilities (Mayakovskaya, Talakhovskaya, Pregolskaya, Primorskaya) is estimated at 100 billion roubles. The projects are being implemented by OOO Kaliningrads-kaya Generatsiya, almost 100% controlled by Rosneftgaz. They will be operated by Inter RAO.³²

The current electricity demand in the Kaliningrad region is up to 830 MW per year. Moscow has indicated that the expansion of the generation capacity by

²⁹ ‘Виктор Зубков: в Калининградской области есть все предпосылки для выхода на новый уровень использования природного газа на транспорте’, *op. cit.*

³⁰ The plans to build two nuclear power plant units with a total capacity of 2,300 MW was suspended in June 2013. For more information on the project, see: J. Rogoża, A. Wierzbowska-Miazga, I. Wiśniewska, *A captive island: Kaliningrad between Moscow and the EU* [series: “OSW Studies”, no. 41], Warsaw 2012, pp. 39–41.

³¹ Е. Вавина, ‘Калининградская область добилась энергетической независимости’, *Ведомости*, 7.03.2019.

³² ‘Газпром планирует развитие в Калининградской области объектов газовой генерации – Миллер’, *Нефтегазовое Обозрение*, 25–31 августа 2016 года, pp. 46–47. ОАО Pervouralskiy Novotrubny Zavod is the supplier of pipes for the Pregolskaya and Primorskaya heat and power plants.

approximately 950 MW is related to the projected increase in consumption in Kaliningrad Oblast by as much as 100% by 2020. In addition, it has been noted that the investments are also intended to provide security in the event that renovation work is needed or it will otherwise be necessary to shut down the existing CHP plants.

The ongoing expansion of power capacity is not merely a part of the strengthening of the region's energy self-sufficiency – it is also intended **at enabling the discontinuation of electricity transmission through Lithuania in the event of the planned desynchronisation of the Baltic states** with the post-Soviet power grid by 2025. Although the energy needs of the Kaliningrad region are already satisfied by local power plants, reserve capacity is being provided by power plants in mainland Russia, which are connected to Kaliningrad Oblast via power grids passing through the territory of Lithuania. The first attempt to operate the Kaliningrad system in isolated mode in 2014 failed. A 72-hour trial of isolated operation of the power system of the Kaliningrad region was successfully conducted in May 2019, as confirmed by Anton Alikhanov on 20th June 2019.³³

2.3. Development of the transport potential

In the last two years **an increase in spending on the transport sector in the Kaliningrad region could be observed**. On the one hand, **the aim of these measures has been to reduce its transport dependence on transit through Lithuania, Belarus or Poland** by expanding the seaports and the airport. On the other, **these investments are intended to make it possible to use the transit potential of the region, particularly for the dynamically growing transport between Asia and Europe**. To this end, development of the railway and port infrastructure of the region had been particularly promoted.

The region tries to make use of its **transport assets**, including the two railway stations in Kaliningrad and Chernyakhovsk located at the junction of standard (1,435 mm) and broad (1,520 mm) gauge tracks, as well as its ports, Russia's only ice-free seaports in the Baltic Sea.

The actions taken so far by the Russian authorities, especially in the last two years, have resulted in the **creation of two transport and logistics centres (TLC) in the Kaliningrad Oblast: in Kaliningrad at the**

³³ 'Калининградская энергосистема успешно прошла тест на работу в изолированном режиме', Переток.ру, 20.06.2019.

Dzerzhinskaya-Novaya station and in Chernyakhovsk, which are capable of transshipping goods from Russian to European wagons and vice versa (see Map 3). In both cases, Kaliningrad Railways (part of Russian Railways) used the existing railway infrastructure, the expansion and modernisation of which has so far cost more than US\$ 5 million. As a result, in 2017, it was possible to reload coal to European rail carriages in the territory of Russia for the first time (so far the reloading was carried out in Poland or Belarus), and to reload containers in transit from Europe to China from European to Russian carriages. Further work is being carried out both on the development of the land railway route through Poland and on the multimodal railway connection from China through Kaliningrad Oblast and further on to the ports of Kaliningrad and Rotterdam. In 2018 test train shipments were carried out on these routes. As a result, rail freight transport increased by about 17% in 2018.³⁴

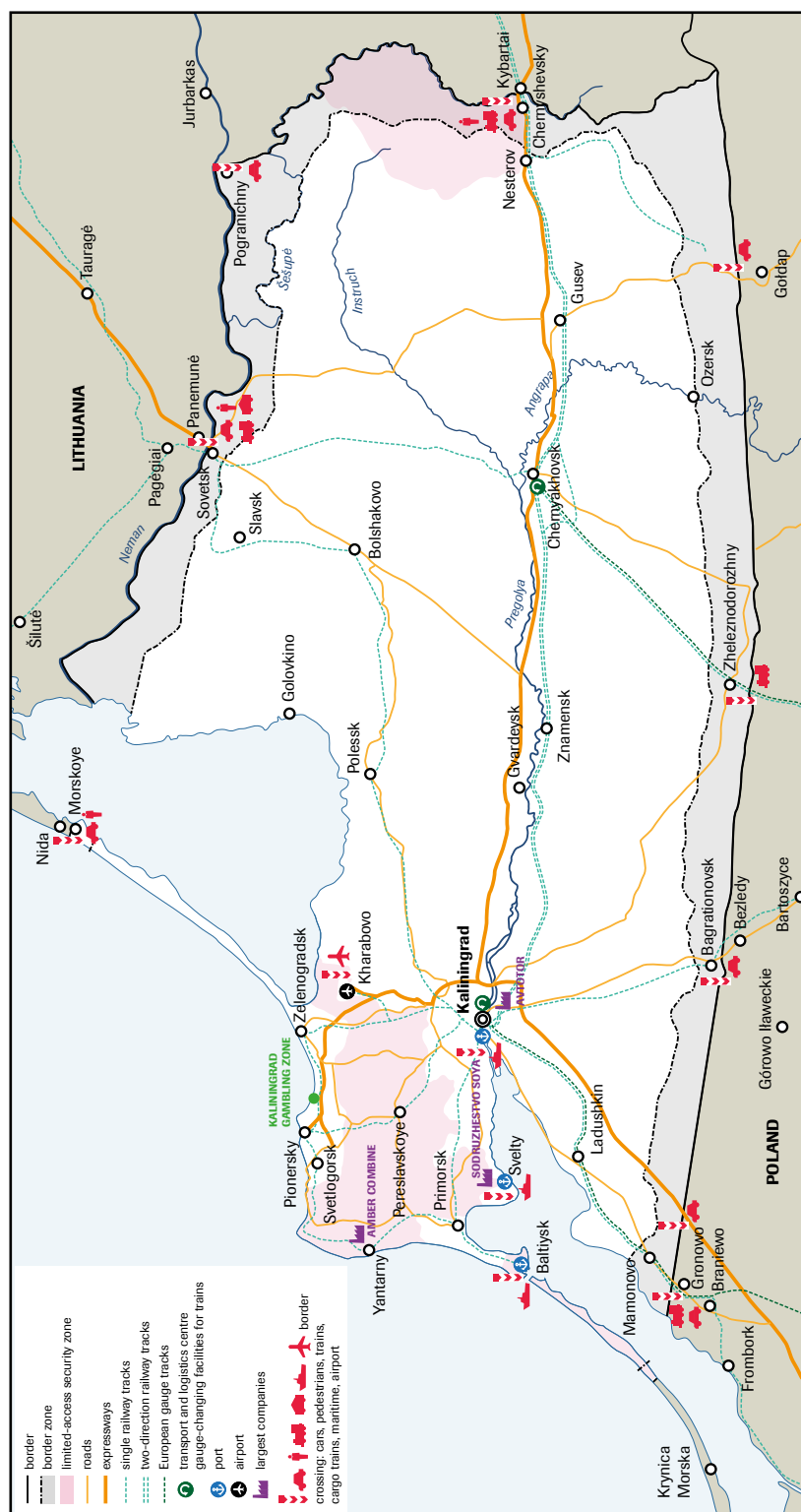
The ambition of the Russian authorities is to create an industrial park around the terminal in Chernyakhovsk which will specialise in transport and logistics, and in the production of building materials. This project, currently in the pre-investment phase, was modelled on the industrial park and dry port in Khorgos on the border between China and Kazakhstan.³⁵

The success of the plans to create a transport hub in the Kaliningrad region will largely depend on the shape of Russia's relations with Lithuania and Poland, through which the trains have to transit. For the time being, the Russian side is conducting talks on railway connections primarily at the business level, i.e. with the other railway companies which would be involved in transit. Moscow's policy on transport tariffs and its readiness to subsidise them is also a key issue for the project. Federal subsidies intended to compensate Kaliningrad entrepreneurs for part of the railway freight tariffs were withdrawn in 2018, as the money was redirected (among others aims) to the construction of new ferries to operate the Kaliningrad Oblast's maritime connection with Russia. It has been estimated that the cost of rail freight transport from/to Kaliningrad through Lithuania and Belarus is about 40% more expensive than transporting goods over the same distance within Russia. For example, the Avtotor factory importing car assembly parts from South Korea has decided not to change its delivery route because, even though train delivery times could have been reduced to 12 days from the current 45 days, sea freight still turned out to cost almost 50% less than rail freight.

³⁴ See: [Калининградская железная дорога 2019](#).

³⁵ See: [Корпорация развития Калининградской области, 2019](#).

Map 3. Transport infrastructure in the Kaliningrad Oblast



The Russian authorities have also taken measures to **improve transport security and the security of supplies** to the region which is dependent on external supplies of raw materials and commodities. This is to be achieved by expanding the port infrastructure and the airport to enable the transport of goods and people without transit. The construction of a **deep-water international freight and passenger terminal in Pionersky**,³⁶ to be commissioned in the autumn of 2019, is another important element in the development of the region's transshipment potential. Worth an estimated 7.3 billion roubles, the project involves reconstructing and expanding the port infrastructure in Pionersky³⁷ with access to the high seas. The terminal will be capable of handling approximately 300,000 passengers per year and up to 90,000 freight vehicles. The new port, which will also be able to accommodate large cruise ships, will primarily help to increase the number of tourists visiting the region.³⁸ The project is being carried out by the Samara-based Bolverk company (owned by Stanislav Loban).

The Russian government is, moreover, considering the construction of a deep-water cargo port in the town of Yantarny. The decision is expected in autumn 2019. The port will have a cargo handling capacity of 48 million tonnes (including a container terminal with a capacity of 35 million tonnes) and is expected to cost RUB 200 billion, of which 50 billion would come from the state budget.³⁹

The incorporation of the Kaliningrad ports into the SEZ in 2018 means that companies registered in the ports are able to benefit from the SEZ's preferential rule. It is also an important factor contributing to the development of the ports' potential and should make Kaliningrad's ports more attractive. Currently only less than a third of their potential is used (they are able to reload approximately 45 million tonnes of goods annually, while in 2017 they reloaded only approximately 14 million tonnes). Kaliningrad's ports are controlled by the state-owned company Rosmorport.

³⁶ See: *Морское строительство и технологии 2019*.

³⁷ Back in Soviet times, Pionersky hosted the USSR's ocean fishing fleet base.

³⁸ The port of Kaliningrad is accessible via a 40-kilometre-long 9–10.5 m deep channel which is not suitable for ocean-class vessels. The port of Pionersky will be connected to the Kaliningrad Oblast's road infrastructure and Kaliningrad will be accessible by an express road. See: Ю. Парамонова, 'Трузопассажирский терминал: может не сработать?', RuGrad.EU, 14.05.2018.

³⁹ А. Веденеева, О. Мордюшенко, 'Новый порт — янтарными темпами', *Коммерсантъ*, 27.05.2019.

The Russian government's decision to build two new ferries to service intra-Russian transport on the Baltiysk-Ust-Luga route has also played a significant role in the development of alternative transport routes: the first ferry is to arrive in the region in 2020 (in 2018, approximately US\$ 80 million was allocated from the federal budget for this purpose). At present, this connection is served by two ferries built back in the 1980s, which often fail. In addition, a significant part of the transport capacity of the ferries is reserved by the Russian Ministry of Defence for the transport of troops and military equipment to and from the Kaliningrad Oblast.

The **expansion of Khrabrovo Airport**, completed in 2018 before the FIFA World Cup, has been very important for increasing regional passenger traffic without the need to use transit routes. The airport is owned by Novaport, a company controlled by the billionaire Roman Trotsenko, who is (among his other roles) an advisor to the president of state-owned Rosneft, Igor Sechin. Khrabrovo Airport is now capable of accommodating aircraft of almost all sizes. In 2018, it handled 2.1 million passengers, i.e. 20% more than in the previous year, and its current capacity is 3 million passengers per year. The ambition of the airport is to become a regional tourist hub and take over some of the traffic currently handled by other airports, especially Gdansk, which Kaliningrad citizens often use to travel around the world. This is why international flights from Kaliningrad have been launched by Pobeda, a Russian low-cost airline belonging to the Aeroflot Group. However, its offer is currently rather modest (Rome and, in the summer season, flights to Paris are also to be launched).

2.4. Investments in the region as a way to fund oligarchs

Several large federally funded infrastructure projects have been carried out in the Kaliningrad Oblast in the last few years, even while the Kremlin was implementing a policy of federal budget consolidation and cutting public spending.

During the implementation phase these projects have undoubtedly contributed to the dynamic growth of investments in the region, providing employment and contracts for many local businesses in recent years. In the longer term, however, some projects, such as investments in the energy sector or the football stadium, will become a financial burden for their investors and the regional budget.

Therefore, it seems that the main motivation behind those projects was, firstly, to strengthen the state's security through the development of the region's

energy and transport potential, secondly, to boost Kaliningrad's international prestige associated with the organisation of the World Cup 2018, and thirdly, to **siphon off state funds to the private accounts of selected oligarchs through the implementation of expensive investment projects financed from the state budget**. The economic development of the region or, more broadly, of the Russian economy, was much less important.

The construction (estimated at 100 billion roubles) of the four new power plants in the region (Mayakovskaya, Talakhovskaya, Pregolskaya, Primorskaya) was carried out by Igor Sechin's Rosneftgaz. Whereas the construction of the floating land part LNG regasification terminal was carried out by Gennady Timchenko's Sroytransgaz. Timchenko is one of President Putin's closest friends (for more information see Chapter II.2.2).

The **2018 World Cup in Russia** has turned out to be the most expensive FIFA World Cup of all time, consuming more than US\$ 13 billion. **Its organisation was largely financed from the state budget and benefited the business environment of the president:** companies controlled by Putin's friends were the main winners of tenders for the construction of sports and transport facilities.⁴⁰ Kaliningrad was one of the eleven cities hosting matches. The **Kaliningrad stadium** was financed from the federal budget. Its main contractor was the state-owned company Sport Engineering controlled by the Ministry of Sport, headed by Minister Vitaly Mutko. It was one of the most expensive in terms of the cost per one seat (even though the construction of a retractable roof was abandoned during the project). Its budget grew rapidly during the construction largely because of its location on the marshy island of Oktyabrsky in the city centre. The final investment cost was about 70% higher than initially planned and amounted to 17.5 billion roubles. Moreover, another 10 billion roubles was spent on the construction of access infrastructure and development of the area around the stadium.⁴¹ However, thanks to this capital-intensive investment, attractive development areas on the island of Oktyabrsky have been

⁴⁰ For more information see: I. Wiśniewska, J. Rogoża, 'The 2018 FIFA World Cup in Russia – circuses instead of bread?' [series: "OSW Commentaries", no. 286], 17.09.2018.

⁴¹ The contract for the eastern flyover connecting Oktyabrsky Island with the mainland, worth approximately 5 billion roubles, was awarded to VAD (under Western sanctions for activities in Crimea) owned by Valery Abramov and Viktor Perevalov. For several years now, the company has been carrying out large public procurement projects, most likely thanks to the support of Arkady Rotenberg, according to the Russian media. For more information about the stadium construction and access infrastructure project: М. Алфимов, 'Самый проблемный стадион ЧМ-2018. На песке украли 750 млн рублей', Sports.ru, 31.03.2018.

expanded, which are currently at the disposal of the governor of the region (a cultural and entertainment complex and a tax haven for companies relocating their operations from abroad are among the facilities that will be created there). Preparation and reinforcement of the terrain for the stadium not only required expanding the budget and extending the project schedule, it also attracted corruption. The Russian oligarch Ziyavudin Magomedov, whose company was responsible for these works, is currently in custody on charges concerning, inter alia, the execution of this contract. However, problems with the stadium had emerged and its costs had started growing already at the design stage, which was finally taken care of without a tender by Crocus International S.A., a company owned by the oligarch Araz Agalarov.

The stadium is to become the property of the regional authorities in 2019, although the federal budget has committed itself to financing most of its operating costs until 2023. The regional authorities argue that **it is impossible to maintain the stadium with revenues from organising matches of Kaliningrad Baltika Football Club or other sports and cultural events, as the government assumes will be the case.** The Ministry of Sport of the Russian Federation has estimated the costs of operating the stadium in Kaliningrad for the years 2019–2021 at 1 billion roubles.

There are also many doubts about the profitability and advisability of another large investment project the Russian authorities are planning in the region: **the construction of a cultural complex on the island of Oktyabrsky.** This will house: branches of the Bolshoi in Moscow and the largest Russian museums (the St. Petersburg Hermitage and the Moscow Tretyakov Gallery), and others. The complex is expected to cost nearly twice as much as the stadium. The contract has been awarded to the Stroygazmontazh company owned by Arkady Rotenberg, one of President Putin's closest friends.⁴² According to estimates by President Putin's advisor Andrei Belousov, the annual maintenance costs of this facility after it is put into operation in 2023 may reach 3 billion roubles, and it has not been decided how this is going to be covered. In the future, the complex may therefore become a drain on the regional budget.

⁴² Similar investments have been planned in Vladivostok and Samara. The total amount of the contract for the three complexes, which Rotenberg's Stroygazmontazh should complete by 2023, amounts to at least 80 billion roubles. For more information, see: Т. Дзядко, 'Музеи от Ротенберга: как бизнесмен зарабатывает на культурных проектах', РБК, 15.11.2018.

THEATRE | CINEMA |
MUSEUM | BALLET

the cultural
and entertainment complex



2.5. Kaliningrad as a tax haven

In July 2018, the Kremlin chose Kaliningrad and Vladivostok as the locations for its “special administrative zones” (SAZ), i.e. tax havens. In Kaliningrad this zone is located on the island of Oktyabrsky (currently the location of the city’s football stadium). Creating the SAZ in Russia is the Kremlin’s idea to support Russian entrepreneurs who have been subjected to Western sanctions and are having difficulties doing business abroad. However, it is a way of encouraging Russian oligarchs to transfer capital that was previously kept in tax havens back to Russia.

Only legal persons who are not from the financial sector and who relocate their operations to Kaliningrad from abroad can become residents of the SAZ in Kaliningrad. They are obliged to invest at least 50 million roubles (approximately US\$ 0.8 million) in Russia (but not necessarily in the Kaliningrad Oblast) within six months of registration. In return, they can benefit from low taxation and simplified inspections. Residents of the zone will be exempt from the tax on the sale of assets and income from dividends, and will benefit from a reduced (5%) rate on dividends from shares of holding companies.⁴³

As of the end of May 2019, eight companies had their headquarters registered in the Kaliningrad zone. Adanimov Trading Limited (previously registered in Cyprus), owned by Omsk businessmen Ilia and Gennady Fridman, was the first to register. In May 2019, seven companies related to Oleg Deripaska, a Russian oligarch who has been subject to US sanctions since April 2018, became registered in the zone: Trans Sektor Holdings, Samolus Investments, Prime Emerald Trading, Fenestraria Consultants, Langdale Holding, Rasperia Trading, Ceratozamia Consultants.

In autumn 2018, readiness to apply for resident status was also signalled by En+ and its controlled aluminium corporation Rusal (of which Oleg Deripaska was also the majority owner until recently). En+ and Rusal were also subjected to US sanctions in April 2018, but as Deripaska reduced his share in these companies to below 50%, in January 2019 the US administration lifted the restrictions on them. However, as of the end of May 2019, the new owners had not applied for the status of zone resident.

⁴³ See: Н. Еремина, ‘Сдавайте валюту: зачем России понадобились офшоры’, Gazeta.ru, 29.07.2018.

III. THE KALININGRAD OBLAST AND ITS EXTERNAL ENVIRONMENT

1. Cross-border political relations

The Kaliningrad Oblast's cross-border relations with the outside world are subordinated to the logic of Russia's authoritarian system of government and the increasingly centralised way in which Moscow has governed the regions for several years. This means that Kaliningrad cannot independently choose the directions and forms of its external co-operation. Its external policy is shaped and controlled by the federal authorities. However, even though the relations between the Kaliningrad Oblast and its neighbours are significantly influenced by the status of the Kremlin's relations with its foreign partners, they are still noticeably better than Russia's intergovernmental relations.

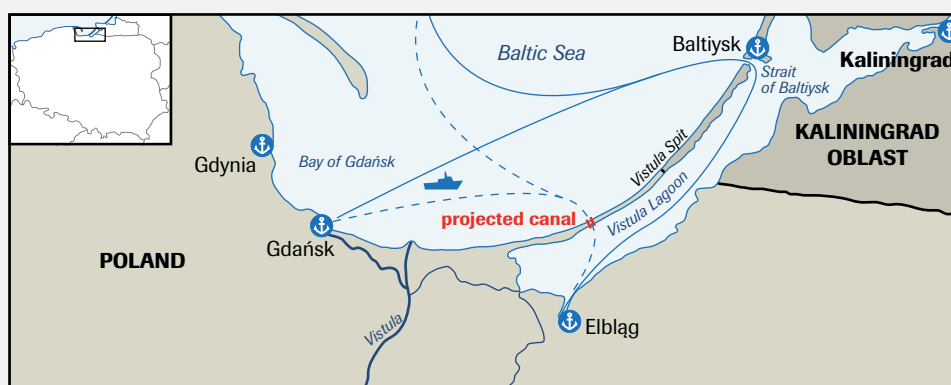
At the state level, the Kaliningrad Oblast's bilateral relations with Poland and Lithuania soured in 2014, the year of Russia's aggression against Ukraine and escalation of its anti-West propaganda. Yet despite the inter-state tensions, bilateral relations between regions have remained correct, even as Poland suspended the agreement on local border traffic in 2016 and stepped up preparations to cut a navigable canal across the Vistula Spit in 2018.

The problem of navigation on the Vistula Lagoon in Polish-Russian relations

As a result of territorial changes after World War II, the territory of the former German East Prussia, including the Vistula Lagoon, was divided between the USSR and Poland. Therefore, **the only waterway connecting the Baltic Sea with the Vistula Lagoon and the port in Elbląg led from now through the Baltiysk Strait, situated entirely within the territory of the USSR.** The rules of navigation through the straits and the Vistula Lagoon were established by the protocol to the Polish-Soviet agreement on the state border of 16 August 1945. In accordance with the protocol, the USSR guaranteed the free movement of merchant ships under the Polish flag to and from Poland in peacetime. Access of third country vessels was subject to the decision of the Soviet authorities. Since July 1991, Poland has been holding talks with the USSR and then with the Russian Federation regarding the signing of a new agreement. Poland has sought, among other things, free access to this waterway for third country vessels. The Russian

side was against this because the port of Baltiysk in the Baltiysk Strait was the main base of the Russian (and previously Soviet) Baltic Fleet. For this reason, and in connection with the plans to develop the port of Elbląg, in 1993 Poland put forward the idea of a Vistula Spit canal to create an alternative waterway, but for a long time this project remained in the sphere of broad concepts. In 2004, Russia tightened the rules for foreign ships to use the route through the Baltiysk Strait, and in 2006 it completely blocked it. Navigation became possible again after the September 2009 signing of the Polish-Russian agreement on the terms of navigation (providing for freedom of movement for merchant ships of Poland and Russia, which could be temporarily restricted on the grounds of environmental or security and defence considerations). Third country vessel traffic was allowed on a limited basis under the unilateral Russian regulation of July 2009, which could be withdrawn at any time. It requires vessels to apply for a permit to pass the straits 15 days in advance. The cost of the permit is 50 euros per vessel. In practice, this system is not being widely used. In 2006–2007 and again in 2016, the Polish government returned to the idea of cutting a navigable canal through the Vistula Spit. In February 2017 the act on this issue was adopted, in December 2018 a tender for the execution of the investment was announced, and in February 2019 a building permit was issued and preparatory works were commenced.

Map 4. Projected Vistula Spit Canal



According to the Polish government's plans, **the navigable canal through the Vistula Spit** is to be built in the area of the former village of Nowy Świat, it will be 1,260 m long, 20 to 60 m wide and 5 m deep. The infrastructure is to include a lock, storm gates, breakwaters, two drawbridges, a parking position and border crossing facilities. The canal will allow the passage of ships and vessels with a length of up to 100 m, up to 20 m wide

and with a draught of up to 4 m. The expected cost of the project is PLN 880 million, and the investment is to be completed by 2022. The official goal of the project is to create a new waterway independent of Russia, connecting the Baltic Sea, via the Vistula Lagoon, with the port in Elbląg. This will allow for the port to be expanded and for increasing revenues from freight transport. The canal is also intended to increase tourist traffic in the region (including sailing) and to improve defence capabilities by allowing access to small naval and border guard vessels.

The project to build a navigable canal through the Vistula Spit on the territory of Poland is causing **negative reactions in Russia**, both at the official level and in the media, although official reactions have so far been limited to the lower political levels. As far as the federal authorities are concerned, in September 2017 the Minister for the Environment and Natural Resources of the Russian Federation, Sergei Donskoy, sent a letter to Jan Szyszko, the Polish Minister for the Environment, calling on the Polish authorities to provide the neighbouring states with comprehensive information on the project and to consult with Russia on its potential harmful consequences before taking a final decision on the implementation of the project. In August 2018, the Deputy Minister for Agriculture and the Head of the Federal Fisheries Agency of the Russian Federation, Ilya Shestakov, sent an official letter to the EU Commissioner for the Environment, Maritime Affairs and Fisheries, Karmenu Vella, complaining that the Polish authorities did not consult the draft with the Russian side, drawing attention to potential environmental and economic threats to Russia and calling for an analysis of the problem and for preventive measures to be taken. In December 2018, a communiqué was published stating that the Minister for Natural Resources and the Environment, Dmitry Kobylkin, had expressed his concern about the project in a conversation with his Polish counterpart Henryk Kowalczyk during the climate summit in Katowice, and had called for an environmental impact assessment and consultations to be conducted. Critical opinions about the project have been expressed by individual members of the Russian Parliament and the Human Rights Council of the President of the Russian Federation (in a statement issued in February 2019).

As far as the Kaliningrad authorities are concerned, in March 2017 the acting governor Anton Alikhanov announced his decision to establish a special working group consisting of 17 people: officials, experts and environmental activists, whose task would be to analyse the (mainly environmental) effects of the Polish project on the region. According to media reports, this

group prepared a report in the summer of 2017 (not published), which was forwarded to Moscow to the Ministry of Natural Resources and the Environment. In his statements, Alikhanov has suggested that the project, which could cause environmental and economic damage to the region, is more of a political, military and strategic project than an economic one, but the regional authorities do not want to “lecture the Poles”, although they do expect them to consult with the Russian side (April 2017). On another occasion he stated that the project may have a negative impact on the environmental situation in the Vistula Lagoon, but the regional authorities are not treating it as a threat (January 2019). Critical views of the project have been expressed by Kaliningrad officials, experts and environmental activists speaking to the media. The Kaliningrad news outlets have provided extensive information about the successive decisions of the Polish authorities concerning the project and have reported on the debate on the project in Poland, mainly quoting critical opinions.

The Russian narrative on the canal project is mainly about environmental concerns. In particular, it has been argued that it will increase the salinity of the waters of the Vistula Lagoon and threaten its populations of freshwater fish (which will cause losses to fisheries in the Kaliningrad region), threaten bird habitats and disturb the migration routes of migratory species, change the layout of sea currents and have a negative impact on the Vistula Spit coasts. In 2017, Russian commentators started to raise security arguments more often. In their view, the canal would contribute to a militarisation of the Polish border area, lead to the creation of new Polish and NATO military installations (some Russian statements allege it concerns, among other issues, the planned reclaimed silt island on the Vistula Lagoon), thus creating new threats to the Kaliningrad Oblast’s military security. Political and legal arguments have also been raised. Poland has been accused of failing to consult the project with the Russian side, despite it negatively affecting the Kaliningrad Oblast. This amounts to a violation of international law, as does the unilateral decision to transform a section of the Vistula Spit into an island (in reality Russia is not a party to the international Espoo Convention on cross-border environmental impact assessments and as such cannot enforce any rights under it and can only rely on the good will of the Polish side).

Despite the worsened relations, both Poland and Lithuania have maintained cross-border contacts with the Kaliningrad Oblast on issues important for both sides, both within the framework of national

cooperation programmes and within the framework of programmes approved and financed by the European Union.

Interregional cooperation between Polish voivodeships (Pomeranian and Warmia-Masuria) **and the Kaliningrad Oblast** takes place within the framework of the Polish-Russian Council for the Cooperation of Regions of the Republic of Poland with the Kaliningrad Oblast of the Russian Federation (the last meeting was held in October 2016 in Olsztyn). Eleven thematic committees operate within the council, including the committees for: border crossings, transport, agriculture, culture, sport, and tourism and environmental protection. Despite the suspension of official contacts at the council level, ongoing working contacts have been maintained, including between border guards.

Contact also takes the form of meetings of: the chambers of industry and commerce, joint economic forums such as the Baltic Business Forum, study visits by municipal government representatives, and joint projects (such as the Gothic castles route implemented jointly with the Pomeranian Voivodeship). In October 2016 (on the occasion of the council meeting) a Polish-Russian forum for business cooperation took place in Olsztyn with the participation of 130 Polish companies, and in December 2016 Kaliningrad hosted the third seminar “Economic Cooperation of Poland with the Kaliningrad Oblast – Warmia and Masuria: traditions and new opportunities for cooperation”, attended by the marshal of the Warmia-Masuria Voivodeship, Gustaw Marek Brzezina and the acting Governor of the Kaliningrad Oblast Anton Alikhanov. During the seminar, the work plan of the Warmia-Masuria Voivodeship and Kaliningrad Oblast for 2017–2019 (including in the field of tourism) was adopted. In April 2018, a delegation of the Olsztyn authorities headed by the mayor of the city, Piotr Grzymowicz, visited Kaliningrad on the occasion of 25 years of cooperation. Every year, the Forum of Partner Regions of the Kaliningrad Oblast takes place in the oblast with the participation of representatives of Poland, Lithuania, Germany, Finland, Belarus, Norway and Estonia. The most recent one was held in Kaliningrad in June 2019. The Forum provides an opportunity for the presentation of the current implementation status of the Poland-Russia Cross-border Co-operation Programme 2014–2020. Representatives of local authorities also meet within the framework of the Forum of South Baltic Parliaments.

Bilateral cooperation is also part of the broader framework of the European Union’s strategy for its Eastern neighbourhood. In 2007–2013, the Lithuania-Poland-Russia cooperation programme was implemented, financed by the European Neighbourhood and Partnership Instrument. In the current financial

perspective for the years 2014–2020, the trilateral programme has been divided into two programmes: Polish-Russian (Poland-Russia Cross-border Cooperation Programme 2014–2020) and a similar Lithuanian-Russian programme.

The Cross-Border Cooperation Programme was launched at the beginning of 2018 (in December 2016 it was approved by the European Commission, and a year later a financing agreement was signed between Poland, Russia and the European Commission). On the Polish side, it involves the Pomeranian, Warmia-Masuria and Podlaskie Voivodeships and, on the Russian side, the Kaliningrad Oblast. The programme's main objective is to promote cross-border cooperation in the social, environmental, economic and institutional spheres. The programme sets out four priorities: cooperation on the conservation and cross-border development of historical, natural and cultural heritage; cooperation on a clean environment in the cross-border area; accessible regions and sustainable cross-border transport and communication; joint actions on efficiency and safety at borders. In January 2019, a meeting of the programme's Joint Monitoring Committee took place in Svetlogorsk. The main objective was to approve the projects submitted under the first call for proposals for the thematic objective "Heritage" (cultural and tourism cooperation, protection of heritage).

In the Kaliningrad Oblast it is possible to learn the Polish language on an optional basis (in a total of ten institutions within the general educational system, half of which are in the city of Kaliningrad), with Polish being taught also by Polish diaspora organisations. The Faculty of Philology and Journalism of the Immanuel Kant University in Kaliningrad offers a course of Polish philology in cooperation with the Consulate of the Republic of Poland, thus playing an important role in the promotion of the Polish language and culture.

As far as **the Kaliningrad Oblast's co-operation with Lithuania** is concerned, a similar Cross-Border Co-operation programme for the years 2014–2020 exists. Its priorities include co-operation in the fields of culture, the protection of heritage, people-to-people contacts, border security, transport and ecology. In 2018 both sides agreed to strengthen cooperation on joint tourist projects and routes.

The negative perception of Lithuania is notable in the narratives of the Russian 'patriotic' communities in the Kaliningrad Oblast (even if this perception is not as strong as that of 'Germanisation'). Lithuania has been accused of inciting separatist tendencies in the Kaliningrad Oblast. The Lithuanian side has

regularly complained about the problems it faces when undertaking efforts to uphold the culture and identity of the Lithuanian national minority in the Kaliningrad Oblast. For example, Vilnius has for years been making unsuccessful efforts to get a full-fledged Lithuanian school established in the oblast. While it is possible to learn Lithuanian in public schools in the Kaliningrad Oblast on an optional basis, teachers of the language from Lithuania face problems obtaining visas or work permits. The authorities are also reluctant to accept direct contacts between school head teachers and Lithuania. At the Kant University, Lithuanian can only be studied as part of the Polish philology curriculum.

2. Cross-border travel

The residents of the Kaliningrad Oblast are more mobile than the average Russian citizen. The percentage of Kaliningrad residents holding passports, according to various data, has been estimated at 60–70% in recent years (28% on average in Russia as a whole).⁴⁴ It is connected with frequent travel to European Union countries, especially to neighbouring Poland and Lithuania, which attract visitors with lower prices and higher quality of food and industrial goods, as well as medical and tourist services. Another reason is that Kaliningrad residents are required to hold a passport to travel to other regions of Russia when travelling by land through Lithuania.

However, the intensity of trips to Poland and Lithuania, and the value of purchases made in these countries by the region's inhabitants, has decreased since 2014. In the aftermath of the annexation of Crimea and the Western sanctions introduced against Russia, **the value of the rouble decreased significantly**, which in turn reduced the purchasing power of Kaliningrad residents and the attractiveness of shopping in EU countries. Two years later (2016) Poland decided to **suspend the local border traffic regime** which had enabled easier and cost-free crossing of the border with Poland – a decision that may have also contributed to the decrease in the number of visitors from Kaliningrad.

In 2015, in the last year of when the local border traffic regime was still in place, the number of crossings of the Polish border by foreigners travelling

⁴⁴ 'Доля имеющих загранпаспорта россиян осталась на уровне 28%', Interfax, 26.04.2016. After the annexation of the Crimea, which resulted in the devaluation of the rouble and an increase in anti-Western sentiment, the number of passports issued both in Russia and in the Kaliningrad region decreased, see: 'Количество выданных загранпаспортов в Калининградской области сократилось вдвое', RuGrad.EU, 7.03.2016.

from Kaliningrad (the absolute majority of whom were residents of the region and Russian citizens) amounted to 2.7 million. In 2017, 2.5 million crossings were recorded, and in 2018 – 2.3 million. An even deeper (and deepening by the year) decrease could be observed in the number of Polish citizens travelling to the Kaliningrad Oblast. The number of border crossings by Polish citizens decreased from 3.3 million in 2015 to 2 million in 2016, 1.4 million in 2017 and 1.3 million in 2018.⁴⁵ The downward trend could not be stopped even by the organisation of four World Cup matches in Kaliningrad in 2018.

Currently, Kaliningrad residents travel to Poland with Schengen visas, mostly multiple-entry visas (in 2018 multiple-entry visas – usually valid for one or two years – accounted for almost 89% of all visas issued by the Consulate General of the Republic of Poland in Kaliningrad). As with the number of border crossings, the number of visas issued by the Consulate General to the oblast's residents has been decreasing. In 2017, it issued 87,459 visas (including 85,447 Schengen visas and 2,012 national visas), and in 2018 this number decreased to 82,211 (including 79,895 Schengen visas and 2316 national visas).

The Consulate General of Lithuania issued 27,730 visas to residents of the region in 2017 and 25,265 visas in 2018 (most of which were multiple-entry and long-stay visas).

After the devaluation of the rouble in 2014, there was a decrease in value of foreigners' purchases declared on the Polish-Russian land border in Poland (which started to rise again only in 2017 as the rouble stabilised). In the case of Polish citizens, the suspension of the local border traffic regime has been the decisive factor that contributed to the decrease in the number of border crossings and the value of purchases in the Kaliningrad region – since then, there has been a significant decrease in visits and spending, which has been increasing year on year.⁴⁶

⁴⁵ Statistics by the Border Guard.

⁴⁶ Statistics Poland, *Ruch graniczny oraz wydatki cudzoziemców w Polsce i Polaków za granicą w III kwartale 2017 roku*.

Table 1. Border traffic and spending by Kaliningrad residents in Poland and by Polish nationals in Russia

	Border crossings (thousands)		Spending (PLN millions)	
	Foreigners	Poles	Foreigners	Poles
2014	3,355	3,357	866	496
2015	2,800	3,300	581	442
2016	3,300	2,000	481	283
2017	2,600	1,400	568	224
2018	2,800	1,600	552	205

In addition, on 1 January 2019, Russian legislation came into force which limits the amount of goods imported free of duty (so-called personal luggage) from 50 to 25 kg per person (30% of the value is charged for „excess baggage”), which may further reduce the scale of purchases by Kaliningrad citizens in the neighbouring EU countries.

The **introduction in July 2019 of free electronic visas** for visits to Kaliningrad Oblast might become an incentive for foreigners to visit the region. Those visas are valid for eight days and issued directly at the border on the basis of an electronic application filed at least four days earlier. The visa facilitations are available to citizens of 53 countries, including Poland and Lithuania.⁴⁷

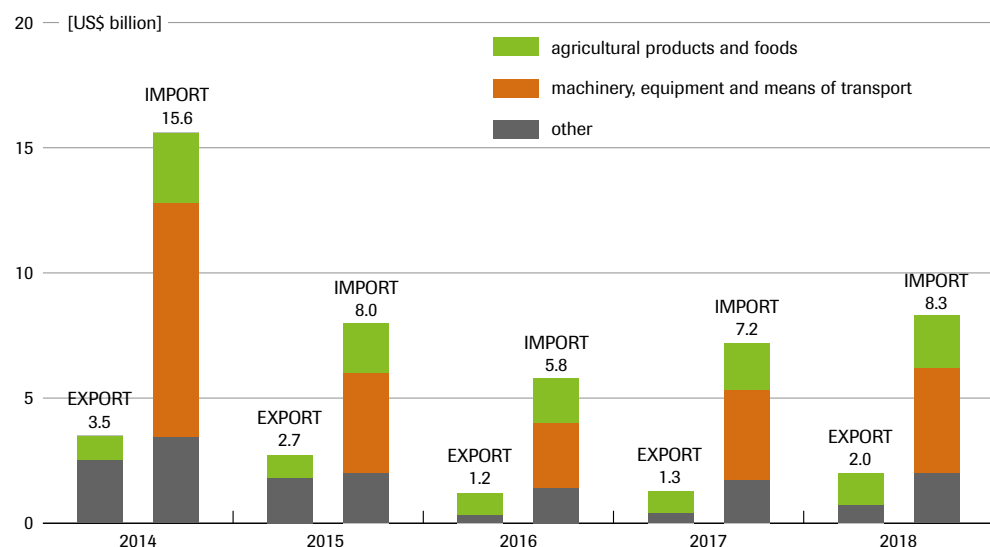
3. Economic relations

The Kaliningrad region is among the top ten Russian regions with the most intensive foreign trade relations. After the collapse of trade in 2015, mainly due to the devaluation of the Russian rouble and, to a lesser extent, the

⁴⁷ ‘Власти опубликовали список стран, граждане которых смогут ездить в Калининград по бесплатной визе’, 27.06.2019. Since August 2017, electronic visas have been issued to citizens of eighteen countries (including China) at the entrance to the Primorsky Krai in the Far East of Russia. During the first year of its operation, over 22,000 people benefited from this solution.

introduction of Western sanctions and Russian counter-sanctions, trade relations have been recovering in the last two years. In 2018, Kaliningrad's exports increased to the equivalent of US\$ 2 billion, i.e. by over 50%, and imports to US\$ 8.3 billion, i.e. by 15%. However, a large negative trade balance remains.

Chart 6. Kaliningrad Oblast's trade exchange



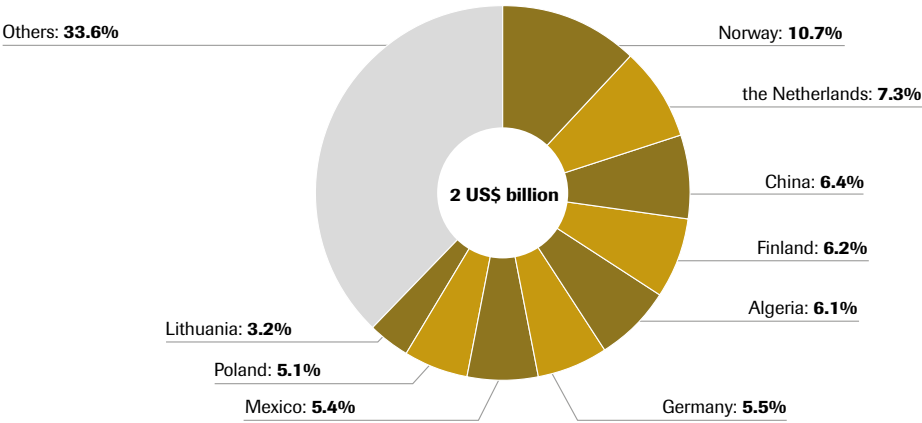
Source: Customs Service of the Kaliningrad Oblast

Agricultural products and foods are the Kaliningrad Oblast's main export commodity, accounting for around 65% of total exports. However, this category of exports has been monopolised by a single company, Sodruzhestvo Holding, which accounts for 90% of the region's total agricultural and foods exports.⁴⁸ This vertically integrated company dealing in the farming and processing of oilseeds as well as trade and logistics is registered in Luxembourg and owned by Alexander and Natalia Lutsenko.⁴⁹ Thanks to the activities of Sodruzhestvo, the Kaliningrad Oblast accounts for around 5% of Russia's total exports of agricultural and food products. Kaliningrad's exports in 2018 went mainly to Norway, the Netherlands and China.

⁴⁸ See: 'Калининградская область увеличила экспорт сельхозпродукции до \$1,3 млрд', TASS, 14.02.2019.

⁴⁹ Lutsenko is a Belarusian by origin, born in East Germany. In 1994 he left his military career for business. In 2014, he commenced construction of the Sodruzhestvo-Soya oilseed processing plant in the Kaliningrad region, which initially processed soya imported from Brazil. In 2018, Forbes estimated his assets at US\$ 0.7 billion. The Lutsenkos (husband and wife) own 90% of the holding company, the remaining 10% is owned by the Japanese trader Mitsui & Co.

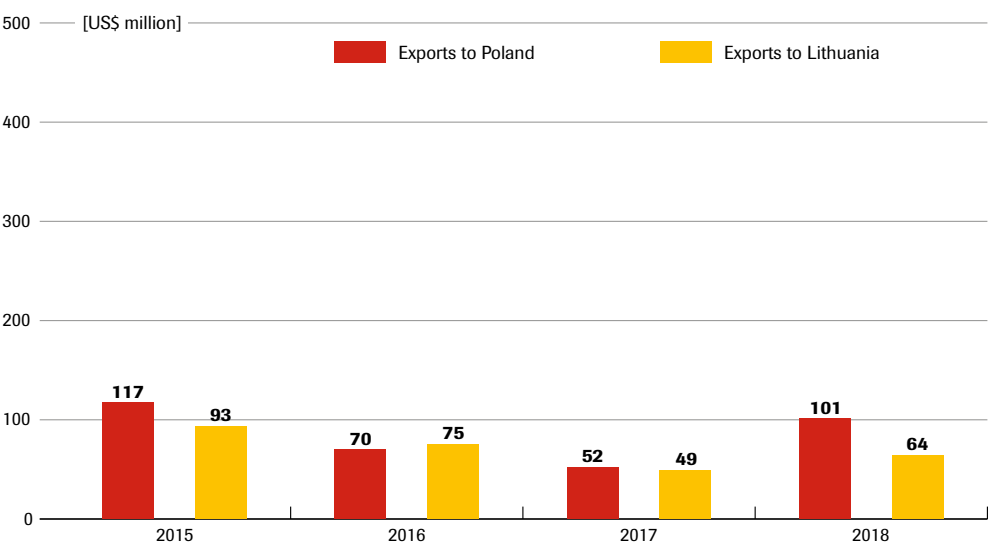
Chart 7. Exports from the Kaliningrad Oblast: the most important destination countries



Source: Customs Service of the Kaliningrad Oblast

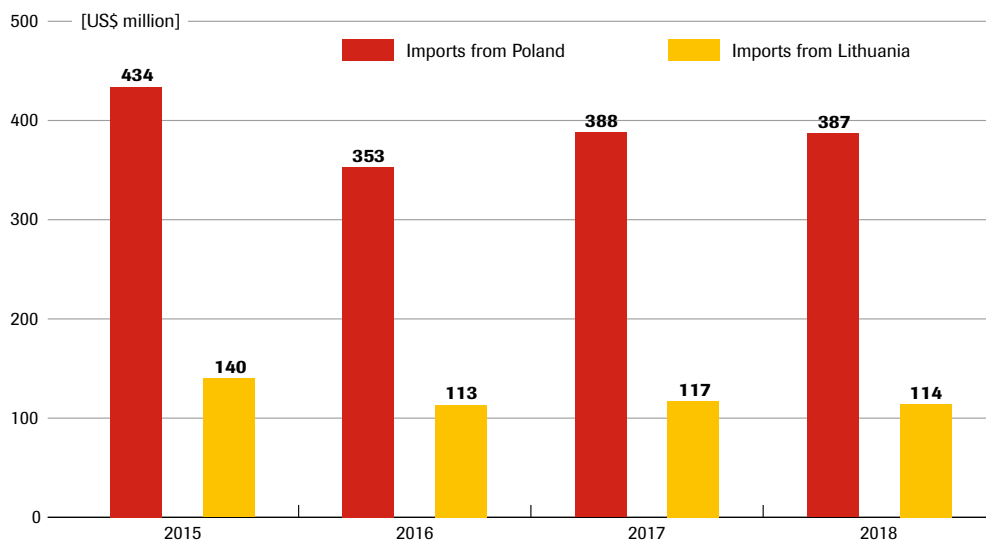
Kaliningrad’s neighbours – Poland and Lithuania – remain important importers of Kaliningrad produce, but despite a gradual increase in purchases in the last two years, the volume of their imports is still much lower than before the crisis. In 2018, Poland purchased commodities worth US\$ 101 million from the Kaliningrad Oblast, making it one of Kaliningrad’s ten largest importers. At US\$ 64 million, Lithuania’s purchases were much lower; the country ranks just outside the top ten importers.

Chart 8. Exports from the Kaliningrad Oblast to neighbouring countries



Source: Customs Service of the Kaliningrad Oblast

Chart 9. Imports to the Kaliningrad Oblast from neighbouring countries

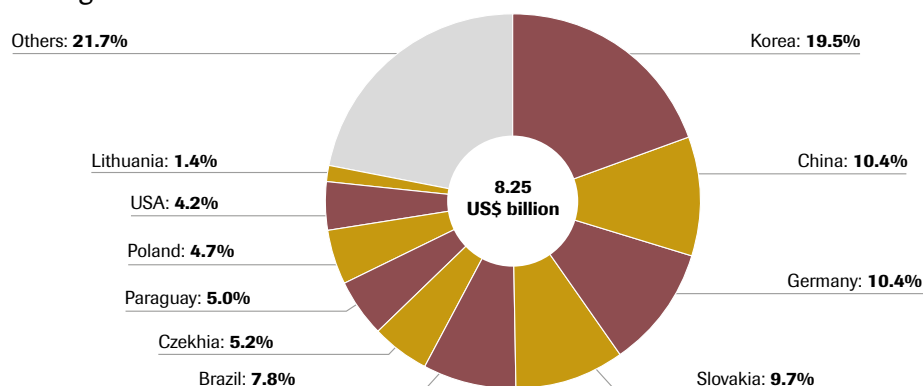


Source: Customs Service of the Kaliningrad Oblast

Imports to Kaliningrad have also been growing rapidly in the last two years. Most of the goods imported to the region belonged to one category: machinery, equipment and means of transport; with car parts and subassemblies made in South Korea, Germany, Slovakia and the Czech Republic for Avtotor accounting for much of the total. Agricultural products and foods still accounted for a quarter of total imports to the oblast. On the one hand this shows the limited effectiveness of the regional authorities' efforts to ensure the self-sufficiency of the region in terms of foodstuffs, and on the other hand is the result of Sodruzhestvo importing a significant amount of cereals for further processing at its plants (e.g. from Brazil or Paraguay).

In 2018, the largest volumes of goods were imported to the oblast from Korea, China and Germany. Poland and Lithuania were also in the top ten most important countries of origin. However, their exports in US\$ terms remained relatively stable in the last three years and in 2018 were worth ca. US\$ 390 million in the case of Poland and almost US\$ 114 million in the case of Lithuania (see Chart 9).

Chart 10. Imports to the Kaliningrad Oblast: the most important countries of origin



Source: Customs Service of the Kaliningrad Oblast

As far as the export of services from the Kaliningrad Oblast is concerned, the transport sector plays a dominant role: it accounted for around 92% of the total volume of services exports (i.e. US\$ 157 million) in the first half of 2018. It should be noted that for now the Kaliningrad Oblast is not able to fully utilise its potential, as a result of which transit via third countries is necessary.

Lithuania's approach is of particular importance for the Kaliningrad transport sector. Lithuania's transit tariffs and policies are the decisive factors influencing the efficiency of the most intensively used connection between Kaliningrad and Russia, which is the land rail route. The need to cross two state borders and use the services of foreign carriers significantly increases the cost of this mode of transport (it is much more expensive, even by as much as 40%, than transport within Russia). Therefore, the level of transit tariffs set in particular by the Lithuanian carrier is crucial. Russian Railways have sought to strengthen their bargaining position by developing an alternative to transit, i.e. the ferry route (see Chapter II.2.3). However, maritime transport is more expensive and slower than moving goods overland.⁵⁰ Experience so far shows that Lithuanian Railways have tended to increase their tariffs when the Kaliningrad ferries were out of order, and when all the ferries were operational, they would lower the tariffs, making the ferry option uncompetitive.

⁵⁰ According to estimates made in Kaliningrad, in the first quarter of 2018 the transport of a coal carriage from the oblast to Russia by ferry was more than 20% more expensive than by land. Cf. В. Хлебников, 'Денег нет: как Москва перестала компенсировать Калининграду его оторванность', *Новый Калининград*, 23.03.2018.

Nevertheless, the importance of Kaliningrad's co-operation with Lithuania and Poland in the rail sector has been growing for the last two years because of Russia's plans to make the Kaliningrad Oblast a transport hub for Asia-Europe-Asia freight. The success of this plan hinges on the readiness on the part of Kaliningrad's neighbours to become more open to rail transit.

Freight connections between the Kaliningrad Oblast and mainland Russia

Around half of the transport services provided by the region concern the transport of goods between the region and mainland Russia. The volume of intra-Russian transport in 2017 was about 6 million tonnes (3.5 million tonnes of imports and 2.5 million tonnes of exports).⁵¹ The land rail links (accounting for approximately 4.5–5 million tons per year) are the main freight transport routes providing supplies to the Kaliningrad region. **There are currently two routes connecting the Kaliningrad Oblast with the rest of Russia:**

- **the northern route** – via Lithuania, Latvia and on to Russia
- **the southern route** – via Lithuania and Belarus; the trains enter Russia on its border with Belarus.

Thanks to the broad gauge track network in Lithuania and Latvia, Russian trains do not have to waste time reloading their goods. However, the necessity to cross two borders and use the services of carriers from the other countries makes the cost of transporting goods by rail from/to the oblast through the territory of Lithuania and Belarus about 40% more expensive than transporting goods over the same distance within Russia.

The direct delivery of goods to the Kaliningrad region from Russia (without going through transit countries) is possible via the **Baltiysk-Ust-Luga sea ferry connection (which is also served by train ferries)**. Currently, this connection is served by two ferries built back in the 1980s, which transport more than 1 million tonnes of goods per year.

⁵¹ Kaliningrad Railway, part of the state-owned Russian Railways; cf. [Калининградская железная дорога](#).

The Avtotor plant located in the Kaliningrad Oblast is the key customer of the Kaliningrad transport sector. In 2017 the company accounted for 69% of container transshipments at the port of Kaliningrad and 65% at the port in Baltiysk, as well 36% of all freight transport by the Kaliningrad Railway. The cars manufactured by Avtotor are delivered to the Russian market mainly by trains, also using the Baltiysk–Ust-Luga train ferry.

IV. SECURITY AND DEFENCE SITUATION AND POLICY IN THE KALININGRAD OBLAST

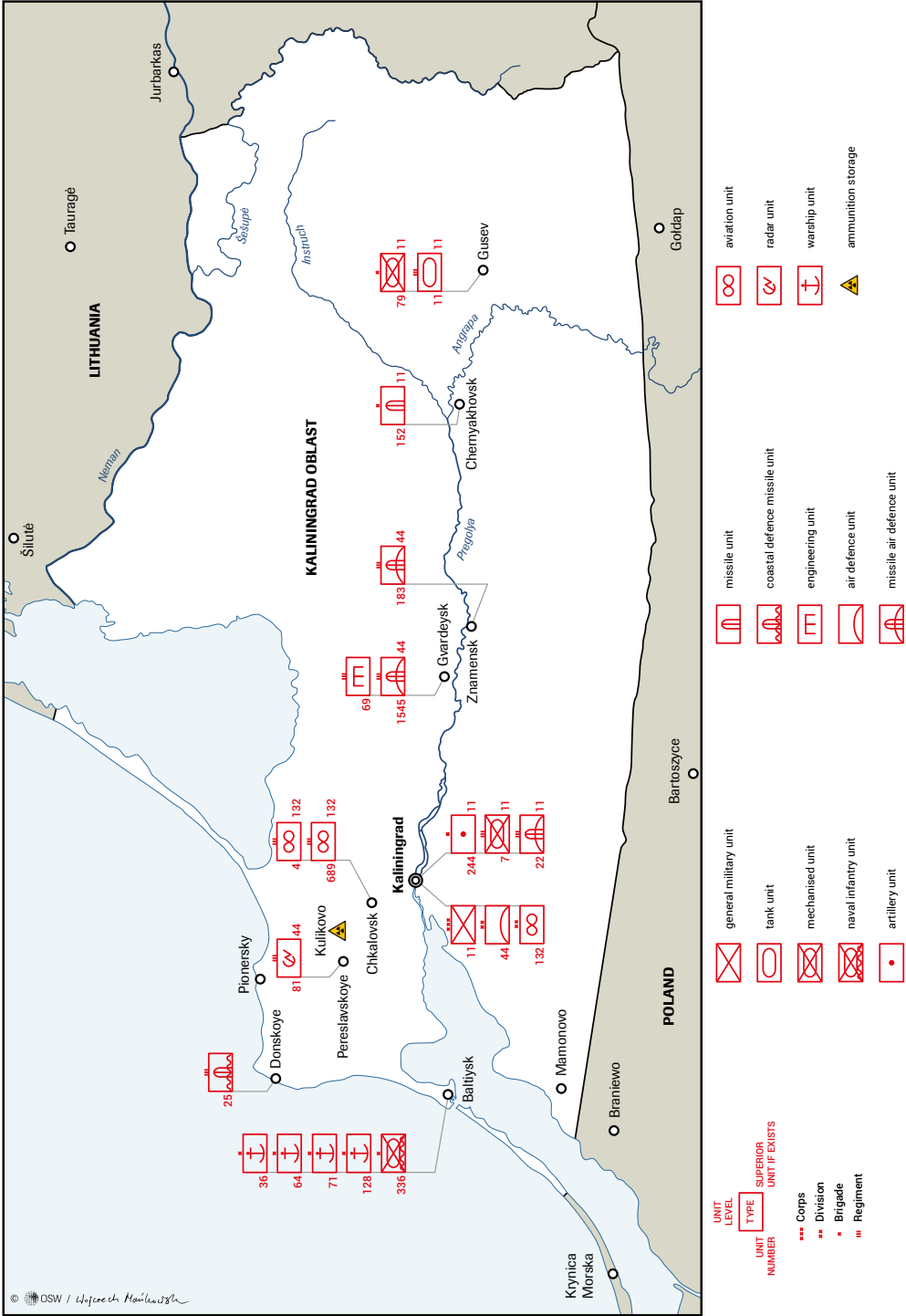
1. Situation within the security institutions and their activities

Because of the Kaliningrad Oblast's strategic location in the Baltic Sea region and the presence of a contingent of the Armed Forces of the Russian Federation, the institutions responsible for internal security, including in the intelligence aspect, are particularly active in the oblast. **The structures of the Federal Security Service (FSB) and the Federal Protective Service (FPS), which are responsible for counter-espionage protection and governmental special communications, play a special role there.** Due to the significant activity of military units stationed in the area, **the activity of FSB military counterintelligence has been increasing. Kaliningrad also remains a base for intelligence operations in Lithuania and Poland.**

The creation in April 2016 of the **National Guard of the Russian Federation (Rosgvardia)** initiated the process of reorganising the units previously comprised in the Internal Troops and special units of the Interior Ministry, including the special National Guard motorised regiment (unit No. 2659) and the OMON units. These structures, apart from fulfilling the current security and protective tasks, are increasingly being involved in the tasks of the Armed Forces. During their training process, particular attention is paid to countering sabotage troops and protecting the Armed Forces' back-up facilities.

Since 2016, a number of reshuffles have taken place in the top leadership of the power and defence ministries' regional directorates. Their characteristic feature has been that posts in the Kaliningrad Oblast were assigned to officers who had no previous links with the region and no contacts with representatives of the local political and business elite. This indicates that **their main task was to make personnel changes in subordinate institutions and to take over control of existing corruption schemes from local entrepreneurs, enforcement institutions and the army.** In 2016, the command of the Baltic Fleet was dismissed for falsifying financial reporting, among others charges. In November 2018, a criminal case was initiated against the former FSB border guard colonel Sergei Radzivil'yuk who had developed illegal financial activities after retiring, embezzled around 5 billion roubles from the accounts of controlled companies and fled to Latvia after his activities were discovered.

Map 5. Main units of the Russian Armed Forces in the Kaliningrad Oblast



In December 2016, Major General Igor Illarionov became the Head of the Interior Ministry's regional directorate in Kaliningrad. It should be noted that prior to his arrival in the oblast, he served as Deputy Chief of Interior Ministry's Directorate for Internal Security, which included him being responsible for secret monitoring of the ministry's officers. The fact that Illarionov was sent to Kaliningrad, which may seem to be a form of downgrading, indicates that the leadership of the Interior Ministry assigned him special tasks, including those related to changing the formula of relations with the local elite, which previously had significant influence on the shape of informal contacts with the local office of the Interior Ministry.

The reshuffles in the **FSB regional directorate in Kaliningrad** were similar in nature. In 2016, when its then head, Yevgeny Zinichev (now Minister for Emergency Situations), was promoted to acting governor, he was replaced as the FSB chief in Kaliningrad by Major General Leonid Mikhailyuk, transferred from Vologda. In the autumn of 2018, after Mikhailyuk took office in occupied Crimea, Valery Belitsky, the former head of the FSB directorate in Kemerovo region, became the FSB's regional chief in Kaliningrad. This string of reshuffles in Kaliningrad's FSB is a strong indication that the **leadership of the service considers the Kaliningrad Oblast to be a region needing special observation.** By periodically replacing the regional chiefs, the FSB seeks to more effectively moderate the internal, secret power relations and prevent a loosening of the headquarters' control of the situation in the region.

In January 2018 Colonel Alexander Nesterenko, who had worked in the structures of the Interior Ministry in St. Petersburg since 1993, was appointed as head of the National Guard regional directorate. Previously, he had served for ten years as chief of the Interior Ministry/Rosgvardia's Extradepartmental Security Service in St. Petersburg (dealing with the provision of paid security services to public administration institutions, museums, courts, etc.). Major General Oleg Gorshkov, Nesterenko's predecessor in the Kaliningrad regional directorate of Rosgvardia (who served between October 2016 and January 2018) currently heads a similar body in the Moscow Oblast.

The law enforcement agencies attach great importance to tasks related to combating 'political extremism' – a concept that encompasses a broad range of activities interpreted as threatening the stability of the system of power. **It is also a unique feature of the Kaliningrad branches of the institutions of force that their work is heavily focused on counteracting activities interpreted by the authorities as aimed at weakening the region's relations**

with Russia. They have succeeded in suppressing the activity of communities advocating cooperation with Germany in various areas, a clear example of which was the closure of the German-Russian House in January 2017. The FSB and the Interior Ministry monitor people with radical views and those critical of the authorities. The activities of the services are continuous and reveal an elaborate system of surveillance. In December 2018, it was announced that a resident of the region who, according to law enforcement agencies was a supporter of nationalist ideology and had established contacts with radical Ukrainian organisations, had been sentenced to eight years' imprisonment. According to the indictment, he had been under surveillance since 2015, because of his activities that were extremist in nature and involved the intention to take up service in an illegal military formation. **The activity of the FSB counter-espionage service has also increased visibly.** In the summer of 2018, the Russian media publicised the case of Antonina Zimina, detained on charges of being a spy for Western intelligence services. Zimina was the head of the Baltic Centre for Cultural Dialogue in Kaliningrad and cooperated with the pro-Kremlin Gorchakov Public Diplomacy Fund. Considering that in 2015 she was expelled from Lithuania where she participated in a conference on international politics, it is possible that she had been cooperating with the Russian secret services. The local FSB also publicises cases of persons who are detained on charges of being involved in military intelligence activities, underlining the preventive nature of its measures. In October 2017, it was announced that a warning conversation had been held with a Kaliningrad resident who intended to provide classified information on the security status of the region to one of the foreign intelligence services.

The Kaliningrad region continues to serve as a base for Russian intelligence activities. This is confirmed by successive reports by the Lithuanian security services⁵² which note the negative consequences of the progressing militarisation of the oblast, considered by Russia as an outpost to counteract NATO's defence capability build-up. Apart from military issues, the Russian intelligence services are also interested in influencing the views of the political elites in neighbouring countries. According to the Lithuanian secret services, Russian intelligence services are involved in inciting activities aimed at encouraging representatives of Lithuania's political and economic elites to promote solutions that facilitate business contacts (including the facilitation of border traffic) and to promote the view that it is necessary to conduct a 'pragmatic' policy towards Russia. **In their**

⁵² See: [National Threat Assessments](#), Vilnius 2018.

intelligence activities, officers of the Russian secret services in the Kaliningrad region use the support of the Belarusian services. In early July 2017, a Lithuanian court sentenced Lieutenant Colonel Nikolai Filipchenko of the FSB to ten years' imprisonment for conducting intelligence activities and attempting to recruit officers from the Lithuanian secret services responsible for the security of government facilities.

2. Military situation in the Kaliningrad Oblast

In 2017–2018 Russia stepped up the modernisation and expansion of military capabilities in the Kaliningrad region, contributing to a visible increase in the offensive capabilities of the Russian armed forces deployed there.

2.1. Expansion of infrastructure

The Kaliningrad Oblast is one of the few regions in Russia whose military infrastructure has not been modernised and developed in any real sense since Soviet times. Expanded in the 1990s to host a contingent of more than 100,000 troops at the peak (when units withdrawn from the Soviet Union's former satellite countries were relocated to the Kaliningrad Oblast), this infrastructure was considered sufficient for the needs of the armed units deployed there – downsized to 25,000 troops at the beginning of the 2000s – and was capable of accommodating potential reinforcements if necessary. **As the infrastructure modernisation process started, it was associated with the progressive professionalisation of troops (and therefore higher requirements from soldiers as to the conditions of service) and, most importantly, with a gradual shift towards new types of weapons and military equipment.** In 2017–2018, **new facilities** for the Iskander missile systems were prepared, with which the 152nd Missile Brigade (Chernyakhovsk) was equipped, as well as for the Bal and Bastion systems, which were provided to the 25th Coastal Missile Regiment (Donskoye). Modernisation efforts were also undertaken with regard to the existing infrastructure for general military units (e.g. for the newly formed 11th Tank Regiment, discussed in more detail below), as well as for the support and logistic backup facilities. Particularly notable is the **reconstruction of the ammunition storage facility (including nuclear weapons), whose reconstruction was completed in mid-2019**⁵³. Satellite images (made available by the US) suggest that the facility, located in Kulikovo near Kaliningrad, has been largely reconstructed.

⁵³ Interfax, TASS, 17.07.2019.

The airfield network has undergone the most significant changes so far. **In October 2018, the modernised and expanded Chkalovsk airfield was finally put into operation** after work commenced in 2012 were completed. **It is now one of the largest military airfields in Russia**, capable of handling virtually all categories of aircraft, including heavy transport planes. The runway has been extended from 2,600 m to 3,100 m and widened to allow the simultaneous take-off of several aircraft, and the number of hangars and parking positions has been significantly increased. The current deployment in Chkalovsk of two fighter aviation regiments recreated in recent years (see below for more information) is presumably not the target solution and should be analysed in the context of the **reconstruction of the Chernyakhovsk** airfield, where all fighter aircraft of the then 72nd Air Base were stationed until the autumn of 2018 in connection with the work on the Chkalovsk airfield. The expansion of the airfield infrastructure should therefore be seen not only in the context of the aforementioned restoration of the two fighter aviation regiments, but also as a basis for the possible transfer of reinforcements in the form of two more fighter aviation regiments to the Kaliningrad region (assuming that the scale of the Chernyakhovsk airfield upgrade will be similar).

2.2. Expansion of the armed forces group

In 2018 the Kaliningrad contingent of the Armed Forces of the Russian Federation **started to expand its air and land units, focusing first of all on the formation of offensive units** – for the first time after decades of cuts followed by stagnation. **Two fighter aviation regiments were reactivated** (part of the 72nd Air Base, since May 2019 the 132nd Mixed Aviation Division), as well as **a tank regiment** (directly subordinated to the command of the 11th Army Corps). The aviation units were recreated on the basis of existing squadrons and expanded, while the tank unit was created from scratch based on personnel and equipment transferred from outside the Kaliningrad Oblast.

The restoration of the 4th Separate Naval Attack Aviation Regiment (stationed in Chkalovsk, before October 2018 in Chernyakhovsk) started in 2017 when the unit received its first deliveries of new Su-30 multirole combat aircraft (see below for more information). The 4th Regiment was created on the basis of the attack aviation squadron of the former 72nd Air Base, which was equipped with older attack and tactical reconnaissance aircraft Su-24M/Su-24MR. In the autumn of 2018, the unit reached combat readiness with two squadrons (Su-24 and Su-30). **The re-establishment of the 689th Fighter Aviation Regiment** commenced in 2018 as the Chkalovsk airfield expansion

was nearing completion. The 689th Regiment was formed on the basis of the fighter squadron of the former 72nd Air Base. Unlike the 4th Naval Attack Aviation Regiment, it is equipped solely with aircraft of the Su-27 family. **As a consequence of the re-creation of the two aviation regiments, the staff and command structures of the entire aviation contingent in the Kaliningrad Oblast were expanded and the 72nd Air Base was transformed into the 132nd Mixed Aviation Division. In addition to the regiments named above, in the 132nd Division a helicopter regiment is being formed.**

In January 2019, the Russian Defence Ministry confirmed that the **11th Independent Tank Regiment (Gusev) had been formed** as part of the 11th Army Corps,⁵⁴ equipped with upgraded T-72B tanks. The unit was created by transforming the independent tank battalion created in July 2018. Upgrading it to regiment status involved the creation of a second battalion, and a third tank battalion and other units of the regiment are expected to be completed in 2019. The 11th Tank Regiment is the first general military unit of this level to be established in the Kaliningrad Oblast since the fall of the Soviet Union. The formation of a tank regiment in the oblast should be seen as **the first, most difficult step towards recreating a mechanised division in the exclave**, because the armoured troops units previously stationed in region had been almost completely disbanded.⁵⁵ Before July 2018, the tank battalion of the 79th Mechanised Brigade (Gusev) was the only armoured unit in the Kaliningrad Oblast.

The plans for 2019 include **establishing an additional (third) missile division (in Donskoye) as part of the 25th Coastal Missile Regiment**, equipped with the Bal systems. When that happens, the regiment will comprise two divisions equipped with the Bal systems and one division with the Bastion

⁵⁴ Bearing in mind the Russian pragmatic approach in which new units start functioning at the onset of a new training period in the Russian Armed Forces (1 December or 1 June), it should be assumed that the 11th Tank Regiment and the 689th Fighter Aviation Regiment were officially incorporated into the structures of the Russian Armed Forces on 1 December 2018, while the 4th Separate Naval Attack Aviation Regiment was probably incorporated six months earlier.

⁵⁵ The remaining general military and support regiments of the 1st Guards Mechanised Division disbanded in 2002 have not been liquidated: one of them continues as a full-fledged unit (currently named the 7th Mechanised Regiment in Kaliningrad), and the remaining two mechanised regiments and the artillery regiment have been transformed into arms and military equipment storage bases. Only the tank regiment and tank battalions in the mechanised regiments were disbanded entirely (the tanks were taken to mainland Russia and the tank battalion in the 7th Mechanised Regiment continues as a cadre structure without weapons).

systems (see below for more information). In addition, it is possible that, after reinforcing, it will be upgraded to a brigade.⁵⁶

2.3. Technical modernisation

Unlike most formations of the Western Military District which it is part of, the Kaliningrad contingent of the Armed Forces of the Russian Federation has long remained on the margins of the Russian military's technical modernisation process. The only exceptions concerned the new equipment acquired by the Navy (new Baltic Fleet warships and auxiliary units, stationed in Baltiysk, have been regularly entering service since 2008) and by air and space defence units. Concerning the latter, S-400 systems were deployed in Kaliningrad in 2013. This was the first deployment of this kind of missile systems in the European part of the Russian Federation apart from the Moscow area. **The Kaliningrad contingent started receiving new offensive weapons only in late 2016.**⁵⁷

The re-arming of the 152nd Missile Brigade (Chernyakhovsk) with the Iskander missile systems, completed in November 2017, has been particularly important, for both military and political reasons. The missiles' nominal range (500 km) covers Poland as well as Estonia, Latvia and Lithuania, and after the launchers are equipped with 9M729 cruise missiles (which is only a matter of time), the whole of Europe will be in the systems' range.⁵⁸ For more than a decade, Russia claimed that the deployment of the Iskander systems at the 152nd Missile Brigade in Kaliningrad would serve as retaliation for US activities in Central and Eastern Europe, and especially the deployment of elements of the missile defence system in Poland, rather than being simply part of the Russian Armed Forces' technical modernisation programme to 2020. Eventually, the Iskanders were deployed in the exclave as originally scheduled, without any relation to the progress of the development of the US base in Redzikowo, Poland, although it should be noted that the 152nd Missile Brigade was the pe-

⁵⁶ In some sources, the 25th Coastal Missile Regiment has already featured for several years as the 25th Coastal Missile Brigade. However, this upgrade has not been confirmed to date and the two-division structure is not consistent with brigade level.

⁵⁷ In the classification adopted in the 1990 Treaty on Conventional Armed Forces in Europe these include: tanks, armoured fighting vehicles, artillery (including missiles systems) with calibres of 100 mm and above, fighter aircraft and combat helicopters.

⁵⁸ Equipping the Iskander systems with 9M729 missiles (based on the Kalibr missiles), which constitutes a violation of the INF Treaty (ultimately terminated by the United States in February 2019 by the United States and then by Russia) increases their range even to 2,600km.

ultimate existing missile brigade in the Russian Ground Forces to receive the Iskander systems.⁵⁹

The provision of the Bastion systems to the second division of the 25th Coastal Missile Regiment (Donskoye) in 2017 should also be considered in a strategic perspective; the first division of the 25th Regiment was equipped with the Bal missile systems in 2016. In 2019 the third division, currently being formed, is expected to receive the systems. The Bal systems, which in principle serve to destroy naval targets, may be armed not only with the Oniks missiles (with a range of up to 600 km), but also with the Kalibr missiles (with a range of at least 1,500 km).⁶⁰ As the operations in Syria demonstrated, both types of missiles can be fired from the Bastion system launchers at naval targets but also at land targets. If the Bastions are used as intended, i.e. as carriers of anti-warship missiles, their deployment in the Kaliningrad Oblast transforms the Baltic Sea (or at least its southern and middle part) into an anti-access zone (A2/AD) which – in the event of an armed conflict – renders navigation difficult or impossible and is comparable to the zone created in the air space by the S-400 systems.

As part of the continuing re-arming of units of the 44th Air Defence Division (Kaliningrad), in 2018 the deployment of the S-400 systems was completed at the 183rd Anti-Aircraft Rocket Regiment (Gvardeysk), and in March 2019, the same systems were provided to the first of the two squadrons of the 1545th Anti-Aircraft Rocket Regiment (Znamensk) that are expected to be armed with the systems this year. **In total, by the end of 2019 the Kaliningrad Oblast will host six full squadrons equipped with S-400 systems (48 launchers, a total of 192 simultaneously fired missiles), putting the region in second position after the Moscow Oblast in terms of the density of the S-400 deployment.** The 1545th Regiment still has two squadrons equipped with the older S-300PS systems but, according to some sources, they have been moved to the reserve in anticipation of re-arming.⁶¹ It should be noted that the replacement

⁵⁹ The original plan was to re-arm 10 missile brigades with the Iskander systems by 2020. In 2015, an eleventh brigade was formed, and in 2018, the formation of two more commenced. By the end of 2018, the Iskander systems had been provided to 11 brigades, most recently to the 448th Missile Brigade (Kursk).

⁶⁰ The range of the Ch-35 missiles of the Bal system is up to 260 km; they are capable of striking waterborne targets only.

⁶¹ The S-300PS divisions were supposed to be moved to the 1545th Air Defence Missile regiment from the 183rd Air Defence Missile Regiment. The S-300W4 systems (two battalions in total) previously held by the 1545th Regiment have probably been decommissioned altogether.

of weapons has taken place in parallel to an expansion of the 1545th Regiment which for many years comprised only two missile squadrons.

In December 2016, Chernyakhovsk saw the first arrival of **new Su-30SM multirole combat aircraft** since the creation of an air force contingent in the Kaliningrad Oblast. In total, by July 2018 the number of this kind of aircraft deployed with the 4th Separate Naval Attack Aviation Regiment had increased to eight, and deliveries are set to continue. According to some sources, the 4th Regiment has also received eight older **Su-30M2** aircraft in order to create a full squadron.⁶² Additional aircraft from the **Su-27** family have also been redeployed to the 689th Fighter Aviation Regiment in the Kaliningrad Oblast from the 790th Fighter Aviation Regiment (Khotilovo in the Tver Oblast) after the latter obtained new **Su-35S aircraft**. However, it has not been confirmed if both squadrons have already reached their full size.⁶³ The Su-27 aircraft of the 689th Fighter Aviation Regiment are also set to be ultimately replaced by the Su-35S.

The **T-72B tanks** which have been deployed in the Kaliningrad Oblast since 2018 are not the most advanced model in the Russian army,⁶⁴ **but the restoration of armoured units in the region should definitely be seen as the most important factor in strengthening the offensive capabilities of the ground troops stationed in the exclave.** Before July 2018, when the first elements of the future 11th Tank Regiment were formed, the Russian Ground Forces in the Kaliningrad Oblast had only 41 tanks (a battalion in the 79th Mechanised Brigade). **When the formation of the 11th Tank Regiment is completed, the number of tanks in**

⁶² Depending on the source, the 4th Separate Naval Attack Aviation Regiment has 14 to 16 machines from the Su-24M family and 8 to 16 machines from the Su-30 family (eight Su-30SM and possibly Su-30M2).

⁶³ Depending on the source, the newly formed squadron of the 689th Fighter Aviation Regiment has 13 Su-27SM3 aircraft of the newest variant or older Su-27P aircraft. Most probably it has both versions of the aircraft, but not necessarily of SM3 standard (according to some sources, the 790th Fighter Aviation Regiment had only six Su-27SM aircraft and the squadron taken over from the 72nd Air Base had 9–10 single-seat Su-27/Su-27P aircraft and 5 two-seat Su-27UP/Su-27UB aircraft).

⁶⁴ There is no information available on the upgrade package of the tanks transferred to the 11th Tank Regiment. Most probably these are tanks of the older standard of T-72B1 (this type of tank was presented in January 2019 to a group of Spanish inspectors), but it should be emphasised that a mass upgrade of the T-72B tanks still held by the Armed Forces of the Russian Federation to the T-72B3 standard – with capabilities comparable to those of the T-90 tank – has been underway for the last several years. It should be assumed that the T-72B3 is set to become the basic tank model also for 11th Army Corps.

the Kaliningrad Oblast will increase to 135.⁶⁵ If the restoration of the tank regiment is a first step towards recreating a mechanised division in the Kaliningrad Oblast,⁶⁶ the recreation of the other mechanised regiments and the planned restoration of tank battalions within the 7th Mechanised Regiment and the 336th Naval Infantry Brigade will result in **an increase in the total number of tanks held by units of the 11th Army Corps in the Kaliningrad Oblast to 300 by the beginning of the next decade.**⁶⁷ The number of armoured fighting vehicles and artillery units will also increase proportionally (see the Appendix).

Compared to the progress made in technologically upgrading the land and air units, the acquisitions of new or modernised equipment for operations on the Baltic Sea in 2017–2018 almost seem insignificant (and it should be remembered that the entire Kaliningrad contingent is directly subordinated to the Baltic Fleet Command and is regarded as the fleet's air and land component). The only exception concerns **the seven modernised anti-submarine Ka-27M helicopters** which the Baltic Fleet acquired by October 2018. This number corresponds to a third of all the land-based anti-submarine helicopters upgraded so far for the Russian Navy, which **demonstrates that preparations to counter NATO submarines in the Baltic are treated as a priority.**

The prototype Karakurt-class / project 22800 missile corvette, the Mytishchi, is the only new Baltic Fleet warship deployed in Baltiysk. It entered service in December 2018 and is armed mainly with Kalibr missiles. **In 2019, the Baltiysk contingent is expected to be reinforced with another vessel of this type – the Sovetsk.**

⁶⁵ A Russian tank regiment (as well as an armoured brigade) comprises three tank battalions (31 tanks in each, including the command tank, making 94 tanks in total), a mechanised battalion (41 infantry fighting vehicles) as well as support and backup units. A tank battalion in brigades and mechanised regiments has one company more (41 tanks in total).

⁶⁶ Armoured and mechanised regiments do not function independently within the structures of the Armed Forces of the Russian Federation. The fact that the 'stand-alone' 7th mechanised regiment was maintained (previously expanded to brigade level) is an indication that there were plans to reactivate a division in the Kaliningrad Oblast, and the creation of the 11th tank regiment further corroborates that.

⁶⁷ A Russian mechanised division comprises three mechanised regiments and one tank regiment. Given that one mechanised regiment (the 7th mechanised regiment) already exists, it cannot be ruled out that only one of the missing regiments would be restored, and the other would be formed on the basis of the 79th Mechanised Brigade. However, the operational characteristics of the Kaliningrad Oblast suggest that the 79th Mechanised Brigade will remain an independent tactical unit.

Four **Steregushchiy-class / project 20380 corvettes** started service in the Baltic Fleet in 2008–2014. The **Neustrashimy-class / project 11540 Yastreb frigate** is being upgraded and this is about to be completed at Kaliningrad's Yantar shipyard. The two **project 877 submarines** that are still present in the Baltic and operate from Kronstadt (expected to be joined by a third vessel of this type, transferred from the Black Sea Fleet to the Baltic Fleet and currently undergoing modernisation). It has been decided that all of these **should all be adapted to be capable of launching Kalibr missiles**. This further confirms that the aim is to transform the Baltic Fleet naval contingent into one supporting land and air operations.⁶⁸

2.4. Training activities

The Kaliningrad contingent of the Armed Forces of the Russian Federation has been one of the most actively involved in various training activities for many years. **Since mid-2017 at the latest, i.e. since preparations to the Zapad-2017 strategic drill, units stationed in the exclave have significantly stepped up their training activity, which has remained as intensive since then.** Irrespective of the season, drills have been taking place in the Kaliningrad firing ranges and on the Baltic Sea, and selected units are in permanent firing range training mode. By the autumn of 2018, twenty-six of them have achieved the status of so-called strike units (in permanent readiness).⁶⁹

Observation of the drills suggests that the Kaliningrad contingent is preparing for a regular armed clash (in the form of a combined operation) with NATO's air, land and naval units. Particularly noteworthy are the first-contact units, i.e. air defence, combat units of the Air Force, missile and radio engineering troops, and the 336th Naval Infantry Brigade (the only Russian naval infantry unit that includes a permanent landing and assault battalion modelled on similar units in the Airborne Troops).

⁶⁸ It is notable that the Kalibr missiles are carried by two 21631 Buyan-M-class corvettes (predecessors of the Karakurt-class), which were redeployed to Baltiysk in 2016. The tasks of project 20380 corvettes and project 11540 frigates (the Baltic Fleet has two vessels of this kind, being the only one in Russian Federation's Navy) also include air defence tasks. They should therefore be treated as complementing the on-land systems and expanding the anti-access (A2/AD) zone on the Baltic Sea.

⁶⁹ Including divisions equipped with the Bastion, Iskander and S-400 missile systems, the Serpukhov corvette carrying the Kalibr missiles, Michman Lermontov and Denis Davydov fast landing craft, a squadron of the 4th Separate Naval Attack Aviation Regiment and battalions of the 79th Mechanised Brigade and the 336th Naval Infantry Brigade.

The most frequently repeated elements of the drills include:

- countering the enemy's means of air attack (aircraft and missiles);
- striking targets deep behind enemy lines;
- countering groupings of naval units;
- detecting and countering submarines;
- carrying out landings behind enemy lines using the combined method (with fast landing craft and helicopters);
- distorting the enemy's command and communications systems.

The training that takes place suggest that it is assumed the Kaliningrad contingent would carry out operations independently of the main forces of the Russian army in the western strategic direction (from Moscow's perspective). The drills include moving aircraft to alternate airfields and removing warships from enemy impact area. The defence manoeuvres developed by the 11th Army Corps suggest that the main task of this unit would be to engage enemy forces. It is notable that the 4th Separate Naval Attack Aviation Regiment, which is formally a unit of the naval air forces, has been practising attacks on enemy land units more often than operations on the Baltic Sea. The September 2018 drill which practised the evacuation, repair and redeployment of military equipment damaged in combat, and the drill on the evacuation of wounded personnel (including by fast boats and helicopters from deep behind enemy lines and from the landing zone to a warship) indicate that these are real preparations to an armed confrontation.

Provocations against NATO forces, which have been occurring at least since 2014 and which usually involve the Air Force (such as violations of airspace, obstruction of identification, dangerous encounters with planes and ships from NATO countries), are now a permanent element of the contingent's activities. In January 2019, responding to the entry of US warships into the Baltic, Russian corvettes armed with the Bastion systems conducted a demonstrative drill to practise the destruction of enemy units, taking aim at the US warships according to some sources.⁷⁰ It is an open question if and when this kind of provocation eventually result in an incident involving a real exchange of fire.

⁷⁰ In February 2018, the newly deployed Bastion systems in the Kaliningrad region practiced the sinking of aircraft carriers, but as the possibility of bringing this category of ships to the Baltic Sea is purely hypothetical, these exercises were purely for propaganda reasons.

CONCLUSION: OUTLOOK

As the Kaliningrad Oblast's governance has been centralised and consolidated in the hands of a governor whose independence from Moscow has simultaneously been limited, the **social and political situation** in the region in the coming years will be heavily influenced by the general trends in Russia. The Kremlin's intention will invariably be to maintain full control of the region and to continue using its geopolitical position for the purposes of its anti-Western propaganda campaign and militarisation.

The governor will be held accountable for the stability of the region, despite his limited ability to influence its main determinants. These include: the dysfunctional economic model and underfunded social policy, the investment climate, activities of the secret services, and external relations. Social discontent or tensions within the regional elite may arise as a result of falling standards of living or further asset takeovers by actors associated with Moscow. In that event, the Kremlin's response will most likely be to intensify repression against selected social groups and the establishment (using anti-corruption campaigns designed for public consumption, and repressive laws adopted at the federal level). As a last resort, the region's leadership may be replaced ahead of schedule, which will not affect the logic of how the oblast is managed from the federal level.

The economic situation in the Kaliningrad Oblast depends heavily on the situation in Russia as a whole. According to most forecasts, the Russian economy is expected to grow moderately in the next few years (by about 1% of GDP in 2019 and 3% after 2020). This means that the gross regional product of the oblast will also increase, although maintaining the 2018 growth rate (ca. 3.6%) may prove very difficult. The factors that have been driving the region's growth will wear off. Rising costs of bank loans and the tightening of the central bank's lending conditions for natural persons, combined with falling incomes, will have a negative impact on demand and thus on the financial results of Avtotor, the largest business in the Kaliningrad Oblast. It is also uncertain if investment demand can be sustained at the current level. Most of the large infrastructure projects that have been driving the Kaliningrad Oblast's economy have already been completed, including the stadium or the LNG terminal. While the federal authorities are planning new projects (including the museum and cultural complex in Kaliningrad or a further expansion of the road infrastructure), public spending will most probably be lower than in the last two years.

In the coming years, the energy and transport self-sufficiency which the Kaliningrad Oblast has recently been pursuing will probably only serve to keep the region secure in the event of rising tensions between Russia and its neighbours, or as a potential instrument to pressure its neighbours. However, it will not completely isolate the region nor cause a discontinuation of the current transit co-operation with neighbouring countries, which is much more economical for Russia than using the maritime route for deliveries to the region. Besides, development of good transport co-operation with Lithuania and Poland is a necessary precondition for Russia to utilise the potential of the transport and logistics centres that have been developed in the Kaliningrad Oblast and to succeed in the plans to create a logistics and transport hub in the region to serve freight transport between Asia and Europe.

It is an open question if federal funding for the Kaliningrad Oblast will continue at the current levels in the coming years (in the form of federal investments or budget subsidies), and the answer will show the extent to which the Kremlin's recently heightened interest in the region is a permanent phenomenon.

As far as **relations with the outside world** are concerned, despite Moscow tightening its grip on the Kaliningrad Oblast, its EU neighbourhood will continue to influence the mentality and lifestyles of the Kaliningrad people, promoting openness, mobility and broadly understood activity. This neighbourhood may also be a factor in making the Kaliningrad Oblast more appealing in comparison to other Russian regions and attracting newcomers from other parts of the Russian Federation and migrants from the CIS countries.

With Russia having implemented electronic visas to the Kaliningrad Oblast in July 2019, the region may expect an increase in the number of tourists. The opening of the deep sea terminal in Pionersky, which will be able to handle large cruise ships, may also contribute to increasing the number of visitors. However, because of the region's underdeveloped tourist infrastructure, and especially the insufficient hotel base and underfunded tourist attractions, one should not expect tourism to become a driver for the local economy.

In the **security sphere**, the Kaliningrad Oblast will continue to be closely watched by the Russian secret services. The need to provide counter-intelligence protection to the armed forces contingent deployed in the region will be a decisive factor in the likely build-up of the FSB presence. This will negatively affect the potential for the unrestrained development of contacts abroad. The oblast will remain an important outpost for the Russian intelligence services

interested in carrying out operations in Poland and Lithuania. As the institution responsible for all aspects of internal security in the oblast, the FSB will have a lot of say in the implementation of the regional authorities' investment plans and in the business activities of individual actors.

The activities taking place in the Kaliningrad Oblast in the **military sphere** suggest that the contingent of land and air forces deployed in the exclave will be enlarged by the end of this decade or the beginning of the next, perhaps even to double the current size. This will be done by expanding the existing formations that remained in Kaliningrad after the cuts in the early 2000s, and by creating new units from scratch. The most important aspect of this effort concerns the re-creation of the structures of the mechanised division, which is a *de facto* offensive unit. The transformation of the naval component of the Baltic Fleet deviates from this general enlargement trend: it is the only military unit that retains its original size and only undergoes qualitative changes. This may suggest that the role of its operations on the Baltic Sea is seen as auxiliary to the land and air operations in the event of a major armed conflict in the Baltic Sea region.

The text was closed in July 2019.

APPENDICES

Appendix 1. Selected social and economic indicators of the Kaliningrad Oblast

	2015	2016	2017	2018
Gross regional product (change in %)	-2.5	2.2	2	3.6 (forecast)
Industrial output (change in %)	-8.8	1.4	1.9	3.1
Agricultural output (change in %)	10.2	-4.9	0.3	9.1
Construction (value of work carried out) (change in %)	10.4	9.2	25.1	43.2
Retail (change in %)	-6.2	-0.7	1.1	5
Inflation (December to December)	11.7	4.7	2.8	4.8
Investments in share capital (change in %)	-3.7	15.5	37.4	-3.9
Real incomes (change in %)	-2.5	-7.5	-1	-1
Real wages (in businesses, change in %)	-9.2	-2.9	0.4	4.1
Bank debts of natural persons (jointly, in roubles and foreign currencies) under con- tract in the Kaliningrad Oblast (beginning of year, RUB billions) (change in %)	69.4 +17%	7.4 -3%	68.7 +2%	79.9 +16% (27% increase by 1 Jan. 2019)
Unemployment (in %)	5.9	6	5.2	4.6
Regional budget revenues (RUB billions)	59	85.5	111	126
of this, support from the federal budget (in % of total budget revenue)	32	51	60	60
Regional budget spending (RUB billions)	70	88	114	124
Surplus/Deficit (RUB billions)	-11	-2.5	-3	2

Source: Rosstat

Appendix 2. Economic situation in the Kaliningrad Oblast as compared to the rest of Russia (2018)

	Kaliningrad Oblast	Russia
GRP <i>per capita</i> (RUB thousands, 2017)	421.5	510.3
Real income dynamics (change in %)	-1	-0.2
Industrial output (change in %)	3.1	2.9
Manufacturing (change in %)	3.6	2.6
Construction (change in %)	43.2	5.3
Retail (change in %)	5	2.6
Inflation (in %)	4.8	4.3

Source: Rosstat

Appendix 3. Kaliningrad Oblast’s trade co-operation with Poland and Lithuania
(US\$ millions)

	2015	2016	2017	2018
Total exports:	2,742	1,239	1,270	1,998
Exports to Poland	117	70	52	101
Exports to Lithuania	93	75	49	64
Total imports:	7,965	5,809	7,209	8,249
Imports from Poland	434	353	388	387
Imports from Lithuania	140	113	117	114

Source: Customs Service of the Kaliningrad Oblast

Appendix 4. Units of the Armed Forces of the Russian Federation stationed in the Kaliningrad Oblast (as of end of February 2019)

(general military and combat support sub-units and their basic weapons in compliance with the Treaty on Conventional Armed Forces in Europe, CFE are specified along with the make-up of the units; colour print signifies units formed and arms provided after 1 December 2016)

Central subordination units

- 1407th Central Artillery Armaments Base – Kaliningrad

Ground Forces (units reporting directly to the command of the Western Military District)

- 82nd Radio-Engineering Brigade – Primorye (part of the unit, the other part is located in the Smolensk Oblast)
- 841st Radio-Electronic Combat Centre – Yantarny

Aerospace Forces

- NN. Radio-Technical Node (Voronezh-DM radar station) – Pionersky
- 26th Measurement Point (Sazhen-TM quantum-optical station, Fazan command and measurement system)

Naval Forces (Baltic Fleet)

Maritime component:

- 128th Surface Ship Brigade – Baltiysk (two project 11540 frigates, four project 20380 corvettes equipped with Kalibr missiles; two project 965A destroyer ships were withdrawn from service in 2016 – *Bespokoyne was turned into a museum ship and Nastoychivy has re-entered service and will be upgraded in 2019*);
- 71st Landing Ship Brigade – Baltiysk (four project 775/775M landing ships, two project 12322 Zubr air-cushioned landing crafts, two project 21820 landing boats, three project 11770 boats and one project 1176 landing boat);

- 64th Maritime Region Protection Brigade – Baltiysk (146th Anti-Submarine Warfare Tactical Group – 6 project 1331M anti-submarine corvettes; 232nd Trawler Division – four project 12650 base minesweepers, six project 13000 and 10750 roadstead minesweepers; 313th Spetsnaz Division);
- 36th Missile Boat Brigade – Baltiysk (1st Missile Boat Squadron – seven project 12411/12411M missile corvettes; 106th Small Missile Ship Squadron – four project 12341 missile corvettes; NN Small Missile Ship Squadron – two project 21631 missile corvettes; **one project 22800 corvette**); **a second project 22800 corvette to enter service in 2019**);
- 342nd Emergency and Rescue Division – Baltiysk (twelve rescue and fire protection units);
- 72nd Reconnaissance Ship Squadron – Baltiysk (two medium-sized project 864 reconnaissance ships, two small project 503M reconnaissance ships);
- 603rd Hydrographic Ship Squadron – Baltiysk (one project 861 hydrographic ship, seven hydrographic boats);
- 51st Hydrographic Service Region – Baltiysk (six hydrographic boats);
- Group of Supply Units – Baltiysk (eleven auxiliary units, including two tankers and eight tugs).

Land component:

- 336th Naval Infantry Brigade – Baltiysk (two marine infantry battalions, one landing and assault battalion, two artillery squadrons; 134 BTR-80/82A armoured personnel carriers, eighteen 122 mm 2S1 Gvozdika self-propelled howitzers, twelve 120 mm 2S9 Nona-S self-propelled howitzers, six 122 mm BM-21 Grad multiple rocket launchers); **plans to restore a tank battalion**;
- 561st Maritime Reconnaissance Point – Parusnoye (two Spetsnaz companies);
- 25th Coastal Missile Regiment – Donskoye (two missile squadrons; four Bal missile launchers, **four Bastion missile launchers**); **a third missile squadron to be developed in 2019 (four Bal missile launchers)**;
- NN. Arsenal – Baltiysk.

Air component:

- a squadron of anti-submarine helicopters from the 72nd Airbase (eventually included in the newly formed helicopter regiment of the 132nd Mixed Air Division) – Donskoye (fourteen Ka-27PL/PS anti-submarine helicopters, **seven Ka-27M anti-submarine helicopters, three Ka-29 helicopters**).

The contingent of Ground Forces reporting to the Baltic Fleet command

11th Army Corps – Kaliningrad – consisting of:

- **11th Tank Regiment – Gusev (two tank battalions; sixty-two T-72B tanks); unit under formation;**
- 7th Mechanised Regiment – Kaliningrad (three mechanised battalions, one tank battalion, a squadron of self-propelled artillery; 85 BMP-2 infantry fighting vehicles, 30 T-72B tanks, eighteen 152 mm 2S3 Akatsiya self-propelled howitzers, twelve 120 mm 2B16 Nona-K towed howitzers; general military battalions with a three-company structure);
- 79th Mechanised Brigade – Gusev (three mechanised battalions, a tank battalion, two self-propelled artillery squadrons, one missile artillery squadron, one anti-tank artillery squadron; forty-one T-72B tanks, 159 MT-LB armoured personnel carriers, eleven BTR-80 armoured personnel carriers, thirty-six 152 mm 2S3 Akatsiya self-propelled howitzers, eighteen 120 mm 2S12 Sani mortars, twelve 122 mm BM-21 Grad multiple rocket launchers, twelve 100 mm MT-12 Rapira anti-tank cannons; general military battalions with four-company structure);
- 244th Artillery Brigade – Kaliningrad (one self-propelled artillery squadron, one missile artillery squadron; eighteen 152 mm 2A36 Giatsint-B towed howitzers, eighteen 122 mm BM-21 Grad multiple rocket launchers);
- 152nd Missile Brigade – Chernyakhovsk (three missile squadrons, **twelve 9K723 Iskander-M rocket launchers**);
- 22nd Anti-Aircraft Rocket Regiment – Kaliningrad (four missile batteries, sixteen 9K330 Tor systems).

Units directly reporting to the Baltic Fleet command:

- 69th Engineer Regiment – Gvardeysk;
- 254th Spetsnaz Radio-Engineering Battalion – Gvardeysk;
- 134th Communication Battalion – Kaliningrad;
- 135th Communication Battalion – Kaliningrad;
- 2574th Weapons and Ammunition Base – Guryevsk/Ryabinovka (the creation of a mechanised regiment is likely);
- 2676th Weapons and Ammunition Base – Cherepanovo (the creation of a mechanised regiment is likely);
- 2652nd Artillery Weapons and Ammunition Base – Prokhladnoye (the creation of an artillery regiment is likely);
- 148th Repair and Construction Battalion – Kaliningrad.

The contingent of Aerospace Forces reporting to the Baltic Fleet command

44th Anti-Aircraft Division – Kaliningrad – consisting of:

- 183rd Anti-Aircraft Rocket Regiment – Gvardeysk (five missile squadrons; thirty-two S-400 missile systems, six 96K6 Pantsir-S1 systems);
- 1545th Anti-Aircraft Rocket Regiment – Znamensk (three missile squadrons; eight S-400 missile systems, sixteen S-300W systems); a second missile squadron armed with S-400 systems to be formed in 2019;
- 81st Radio-Engineering Regiment – Pereslavl'skoye.

Units directly reporting to the Baltic Fleet command:

- 132nd Mixed Aviation Division – Kaliningrad – consisting of:
- 4th Separate Naval Attack Aviation Regiment – Chkalovsk (one bomber-reconnaissance squadron, one squadron of multi-function fighter aircraft;

sixteen Su-24M/Su-24MR bomber and tactical reconnaissance aircraft, eight Su-30M2 multirole combat aircraft, eight Su-30SM multirole combat aircraft);

- 689th Fighter Aviation Regiment – Chkalovsk (two fighter squadrons; fourteen Su-27/Su-27P/Su-27UP/Su-27UB fighter aircraft, thirteen Su-27SM3 multirole fighter aircraft);
- transport squadron of the 72nd Air Base (undergoing transformation, a helicopter regiment of the 132nd Mixed Air Division being formed) – Khrabrovo (twelve Mi-24 combat helicopters, eight Mi-8 combat support helicopters, three An-26 transport aircraft, two An-140-100 transport aircraft);
- 81st Communication and Radio-Engineering Battalion – Primorsk/Lunino;
- 82nd Communication and Radio-Engineering Battalion – Kaliningrad.

Appendix 5. Expected expansion of general military and support units at battalion/squadron level and their offensive weapons (basic categories as per the CFE Treaty) following the creation of a mechanised division in the Kaliningrad Oblast

	December 2016	February 2019	2021 (forecast)
Number of general military and support units in the 11 th Army Corps and 336 th Naval Infantry Brigade			
Tank battalion	1/1*	3/1*	8
Mechanised battalion	6	6	13
Naval infantry battalion	2	2	2
Landing and assault battalion	1	1	1
Artillery squadron	8	8	13
Number of offensive weapons (basic categories as per CFE Treaty)			
Tanks	41	103	299
Armoured fighting vehicles	342	342	667
Artillery with calibre of 100 mm and higher	144	144	234

* tank battalion of the 7th Mechanised Regiment existing as a cadre structure without weapons