

Putin's grand design to destroy the EU's Eastern Partnership and replace it with a disastrous neighbourhood policy of his own

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In a surprising *volte face* at his meeting in Moscow with President Putin on September 3rd, President Serzh Sargsyan of Armenia agreed to join the Russian-dominated customs union with Kazakhstan and Belarus. Thus, in one short meeting, he scrapped the draft Association Agreement with the EU, which included a 'Deep and Comprehensive Free Trade Agreement' (DCFTA), whose negotiation over the past three years had advanced to the point that its initialling was firmly scheduled for the Eastern Partnership summit in Vilnius in November. And, at the same time, the Armenian President chose to deprive his country of the possibility to enter into free trade area agreements with other states, which any economy is free to do unless it is part of a customs union, in which case it becomes bound to a common external tariff.

This latter deprivation is particularly serious in Armenia's case, since Russia's external tariff is on average rather highly protective. In the process, Sargsyan has also precluded Armenia from pursuing the only plausible strategy to become an open, highly-skilled, small economy, following for example the model of Israel, with which it shares several features in common. More broadly, it is worth noting that most of the world's top-ten economies by GDP per capita, from Luxembourg to Singapore, are small but completely open countries.

The economic case against joining the Russian customs union is all the greater because nothing in the DCFTA with the EU would have prevented Armenia from entering into a 'high-quality', free trade agreement¹ with the Russian-led customs union. Armenia is already party to the matrix of CIS free trade agreements, but many of these do not function well. Rather than join the Belarus, Kazakhstan and Russia customs union, why should Armenia not simply negotiate a high-quality free trade agreement with it?

President Sargsyan has offered two main explanations for his baffling behaviour: Armenia depends on Russia to guarantee its security and its large diaspora in Russia make it natural for the two countries to have a close economic relationship. One might challenge the first explanation by noting that no other collective security arrangement, e.g. NATO, requires its member states to join a customs union led by the principal nation.

¹ 'High quality' means free trade with no exceptions. The concept is now explicitly developed in South-East Asia by some ASEAN countries with New Zealand, and forms a core principle of the newly emerging Trans-Pacific Partnership (TPP).

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As regards the Armenian diaspora in Russia, their remittances are indeed important to the Armenian economy and will remain so until it becomes dynamic enough to induce its émigrés to return home. During the period of very tense Russian-Georgian relations before their 2008 war, discriminatory measures were employed by the Russian police against Georgians in Russia. Armenia is vitally concerned that its people are not similarly mistreated in Russia. But again, the linkage with the Russia-led customs union is entirely gratuitous and logically unnecessary. For example, both Norway and Switzerland are completely integrated into the EU's labour market and there is the free movement of people throughout the European Economic Area. But the EU sees no need to put pressure on these countries to join its customs union, and both Norway and Switzerland are free to pursue their own trade policies with third countries.

Russian control of gas imports to Armenia may be a further explanatory factor in President Sargsyan's decision. He will surely have observed how Russia uses energy supplies as an instrument of coercive foreign policy in both Ukraine and Moldova.

There are other recent developments that may shed light on Russia's behaviour towards Armenia. On August 13th President Putin made his first visit to Baku in many years, which resulted in contracts for the supply of Russian military hardware to Azerbaijan, amounting to \$4 billion. Azerbaijan itself is greatly expanding its military spending on the basis of its oil and gas revenues and one frequently discerns in the country's political discourse a strong determination to get the settlement it wants over Nagorno-Karabakh, preferably by negotiation, but if necessary, by force. Meanwhile Russia has a military base in Armenia. Thus Russia is conspicuously arming Armenia's enemy while at the same time pressuring it to join the customs union. The precise terms of the Sargsyan-Putin conversation on this matter are not publicly known but left to the imagination.

On the other hand, there are perceptions in Armenia that the EU, while deepening its civil cooperation with Armenia through the Eastern Partnership, has done precious little to ease the country's vulnerable geo-political and geo-economic situation. For example, it has urged Armenia to close its nuclear power station without offering alternative energy solutions. And it has had no perceptible influence over Azerbaijan with a view to resolving the Nagorno-Karabakh conflict or over Turkey on the issue of opening the Armenian-Turkish border for normal transport links.

But this Armenian story is only a part of a grander Russian campaign to also dissuade Ukraine and Moldova from signing their DCFTAs with the EU. Russia has a long track record of using pseudo technical barriers to trade as instruments of political pressure. On September 11th, Russia changed tactics from threat to action by banning all imports of Moldovan wine. Overnight Russian officials transformed what had been an enjoyable alcoholic beverage into a "health hazard" for the entire Russian population. Georgia has suffered similar actions against its wine and sparkling waters at various times in recent years. Currently Ukraine, which routinely is targeted with long customs delays, has been hit with the latest *bijou* of Russian trade diplomacy: Ukrainian chocolates have suddenly been declared a "health hazard" for the whole of the Russian-Kazakh-Belarus customs union! Such actions are contestable at the WTO unless the justification for them is transparent and scientifically proven, which signals another problem: Russia may think that it, as a new member of the WTO, can overrule the rules whenever it has a political interest to do so. .

Moreover, the status of the customs union itself is still uncertain. It cannot be recognised by the WTO or brought under WTO rules since Kazakhstan and Belarus are not yet members of the WTO. Kazakhstan is negotiating accession, but whether it accepts Russia's WTO-bound tariffs as its own is not yet clear. It has signalled that it would like to revise these rates downwards for itself and the whole customs union. Also Kyrgyzstan, which is already a

WTO member, is considering joining the customs union, but this would mean raising its WTO-bound tariffs and thereby entail compensating third countries, which it can hardly afford. More profoundly for Kazakhstan, Kyrgyzstan and other Central Asian republics, it would mean serious tariff barriers with their even-larger neighbour, China, thus certainly causing an increase in the cost of living, since Russia is not a competitive supplier of the goods they import from China. While for the EU's Eastern partners the optimum formula is to have high-quality free trade with both the EU and Russia, for the Central Asian states there is the equivalent case for free trade with both Russia and China, or at least as liberal trade with China as they feel is in their best interests.

President Putin is thus doing all he can to expand his customs union with coercive measures, denying the economic interests of the targeted states for more open economic relationships with the rest of the world, and with the EU in particular. Kazakhstan, while a founding member of the customs union, resents the high level of Russian tariffs it was forced to adopt. In short, a triple disaster is in the making on the European continent: destruction of the EU's benign neighbourhood policy, poisoning of Russia-EU relations and construction of a disastrous Russian neighbourhood policy. Why disastrous? For the EU and EU-Russia relations, it is obvious enough. But how might it harm Armenia, or Moldova or Ukraine? Because the Russian strategy is built on two fatal foundations: first, it would cut off the new member of the customs union from the freedom to develop an open competitive economy in the 21st century's world of globalisation, and second, it would have been built on crude hegemonic geo-political coercion. In combination, they are a recipe for resentment and ultimately failure.

Georgia was thought to have been sufficiently immunised against Russian pressures to join the Russian-led customs union. Recently, however, Prime Minister Bidzina Ivanashvili has created some confusion by saying that he would consider whether the customs union would be in Georgia's interests. This would mean overturning the country's fundamental achievement of becoming completely economically open to the whole world. His remarks, however, were quickly followed by official statements that Georgia's European and Western priorities were not in question. It seems that the Prime Minister was addressing some would-be diplomatic remarks towards Russia, which were reported out of context and should not be over-interpreted.

What can be done? On September 11th, Commissioner Stefan Füle voiced his concerns before the European Parliament acknowledging "enormous pressure being brought to bear" on some of the EU's Eastern partners. The Commissioner declared: "Let me be clear: the development of the Eurasian Economic Union project must respect our partners' sovereign decisions. Any threats from Russia linked to the possible signing of agreements with the European Union are unacceptable." These include citing the misuse of energy prices, artificial trade obstacles, military cooperation and security guarantees and the instrumentalisation of protracted conflicts as unacceptable (see "Commissioner Füle statement to EP Plenary on the pressure exercised by Russia on countries of the Eastern Partnership", 11/09/2013 (http://europa.eu/rapid/press-release_SPEECH-13-687_en.htm)).

The EU now needs to follow up its statement by intensifying its support for Armenia, Moldova, Ukraine and Georgia with a strong information campaign. It needs to explain why the Russian strategy is so dangerous, addressing these arguments to all democratic forces, both political parties and civil society, within the partner states, and notably within Armenian society.

The EU has already started preparations to help Moldova overcome the Russian ban of its wines. In his remarks to the European Parliament, Commissioner Füle reported that he and

the Commissioner for Agriculture “intend to look into the possibility of being able to further increase the wine quota for Moldovan exports to the EU”.

These multiple disasters could be avoided, with benefits to all parties. Russia could expand the reach of its new customs union by entering into high-quality free trade agreements with the states that want also to have DCFTAs with the EU. In addition, Russia and the EU could open discussions over a free trade agreement between the customs union and the EU itself. These steps would be worthy of such expressions as our common European home, where the aim should be the establishment of a common economic space from ‘Lisbon to Vladivostok’ (Putin’s idea). Russia should be willing to make a concordat with the EU, best starting tomorrow, to develop mutually supportive and non-coercive policies towards their common neighbours, rather than insist on playing 19th century zero-sum games of geo-political competition, forcing a choice upon our neighbours who would like good relations with both EU and Russia.

What has to be hammered home to those unsure of the economic arguments is that you do not have to have an exclusive customs union to enjoy deep integration for goods, services, people and capital, and of course even less for hard security relationships. High-quality free trade agreements are the logical instrument for those who want excellent relations with more than one big neighbour.