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New Russia's Strategic Choice: Regionalisation versus Globalisation

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Key Points

* Several factors militate against Russia succeeding in a globalised economy:
    * climate and geography
    * an unbalanced economy unattractive to investors
    * demographics.

* An economic crisis is therefore inevitable.

* Developing a regionalized economy with Central Asia is Russia's only option.

* It balances Russian deficiencies and would provide a basis for developing Siberia and the Russian Far East.

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The period spanning the end of 2003 and beginning of 2004 is likely to go down in the recent history of post-Soviet Russia and a number of Commonwealth of Independent States (CIS) countries as a time extremely rich in landmark political events initiated by Moscow.

On the one hand, this refers to a chain of events inside Russia such as the arrest of the richest of the oligarchs, M Khodorkovskiy, head of the YUKOS oil company, in October 2003; the departure of the President's chief of staff, A Voloshin, a member of the "Yeltsin family" and a bitter opponent of integration in the post-Soviet space[1] in October 2003; the crushing defeat of the liberal parties in the parliamentary elections of December 2003; and, finally, the unexpectedly sudden dismissal of the Kas'yanov government, noted for its liberal views, in January 2004.

On the other hand, a series of events has occurred in the post-Soviet space itself, such as the signing of the Agreement on the Establishment of a Single Economic Space by Russia, Ukraine, Belarus and Kazakhstan at the CIS Summit in Yalta on 19 September 2003, and, following on the heels of Putin's re-election to a second term as President, the meetings held in extremely rapid succession in April 2004 between the Russian leader and the leaders of the CIS's three largest and most influential countries: Uzbekistan, Kazakhstan and Ukraine. Moreover, at their meeting on 28 May in Astana, the Central Asian Cooperation Organization (Kazakhstan, Kyrgyzstan, Tajikistan and Uzbekistan) declared its intention to form a common market and free trade zone and invited Russia to become a member.[2]

What do such apparently diverse events have in common? We believe that what connects them is that they are all characteristic indicators of a profound crisis in Russia's former economic strategy aimed at integration into the world market (globalization). At the same time, they are all equally revealing signs of the shaping by Moscow of the elements of a new strategy aimed at speeding up the processes of integration within the CIS (regionalization). This is, however, undoubtedly only the upper, above-water part of the iceberg that is modern Russia. The authors of this paper have attempted to reveal the main part that lies underwater by analysing the principal factors governing economic activity in Russia and what we see as the inevitability arising from this of Moscow's "economic return" to the CIS and, above all, to Central Asia (Kazakhstan, Kyrgyzstan, Tajikistan, Turkmenistan and Uzbekistan).[3]

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Introduction

Times occur in the history of any country at which life itself forces it to make the decision to undertake a thorough review of its economic development strategy. This usually happens when the old strategy has run its course or has proved to be deeply flawed. We believe that Russia today is at such a point.

The main reason for this is the ever more obvious crisis in the strategic policy adopted back in the early 1990s of doing everything possible to integrate into the world economy. The foundations of this strategy were laid immediately after the disintegration of the USSR, when the Gaydar "reform government" began in effect to deny the need for a state industrial policy and started rapidly to shed the "burden of the national republics". At that time hopes were pinned on opening up the Russian market to the world in order to attract foreign investment. It was assumed that after integration into the world economy foreign capital would pour into Russia, producing an economic leap forward.

However, these experiments proved to have quite the opposite effect: instead of being enriched, the country was drained. In fact, the early 1990s saw the peak of a massive outflow of capital from Russia in the form of raw materials, financial resources, intellectual property and skilled human resources. To all appearances, Gaydar's team failed to appreciate (or were unwilling to appreciate) a simple economic law: capital always gravitates to where it will produce the maximum profit. And in the global market environment Russia has never been, nor can be, such a place.

All this has been gradually dawning on Russia's current leadership. There is no other way of accounting for the fact that a visible stepping-up of efforts to review the former economic development strategy has accompanied Putin's emergence at the foreground of the Russian political stage. The Kremlin is primarily seeking to strengthen the role of the state in the management of the economy and achieve a turnaround in the trend for a massive flow of capital out of the country. The most conspicuous recent evidence of this is the sudden dismissal of Mikhail Kas'yanov's government. We think it would not have occurred to Putin, literally on the eve of the presidential elections, to dissolve the government prematurely if it had really been pulling the country's economy out of crisis, and even less so if it had been ensuring steady growth.

But will these measures be sufficient? For no administrative measures, however radical, can halt the objective processes of the destruction of the Russian economy. Although many Moscow politicians and the provincial media have recently been talking a great deal about Russia's emergence from crisis, this is no more than a propaganda smokescreen.

An important indicator of the economic enfeeblement of Russia is that strategic raw materials – fuel, non-ferrous metals, mineral fertiliser – continue to be shipped out of the country in large quantities. Moreover, the foreign currency earnings from the sale of resources are also being exported instead of invested in Russian productive activity. According to a very wide range of assessments, the export of financial resources from Russia is still reaching at least $20 bn per year (in the early to mid-1990s the figure was in excess of $25 bn).

All this testifies to the continued inertia of Russia's gravitation towards the world market. It is this that is continuing to weaken the Russian economy and to minimize Moscow's political influence in the world. In our view, this cannot fail to arouse mounting concern within the President's administration, the new government and Russian public opinion, and in consequence it will lead them to seek effective ways of pulling the country out of its systemic economic crisis. Sooner or later this will culminate in Moscow's undertaking a thorough and radical revision of its economic development strategy.

In this paper, then, we incline towards the view that the near future will very probably see the following scenario for Russia's development and for processes of integration in the CIS. Firstly, the Russian leadership will soon conclude, if it has not already, that Russia's lack of success in attempting to integrate into the world economy is objective in nature. The consequence will be a decision by Moscow to limit its participation in the world economy.

Secondly, as its most probable next step Russia will do its utmost to boost the creation of a single economic space in the CIS, and some signs of this can already be observed. In this context Moscow is most likely to pin its main hopes on speeding up the processes of integration with the Central Asian countries as the ones of greatest value to Russia.

Should Russia continue its policy of full-scale globalization, then we believe there can only be one alternative to the scenario outlined above, namely disastrous consequences for Russian statehood, comparable in scale to those that led to the Communist revolution in 1917. Objective economic reasons exist for all of this.

Russian Economic Conditions

A Harsh Climate

Because of the long cold winter the organisation of any economic activity in Russia, including the production of raw materials, the building of enterprises, the operation of productive capacity and infrastructure and labour costs significantly more than in many other countries.

Russia currently consumes five to six times as much energy per unit of GDP as the European countries and 12 to 16 times as much as the USA and Japan,[4] since the leading transnational corporations locate their manufacturing in places with much more favourable climates and use energy-saving technologies. Even the production of fuel is considerably more expensive in Russia. Thus, oil production costs an average $1-1.5 per barrel in the Middle East, whereas in Russia the figure is almost ten times as much, at $12-14 per barrel.[5] The same applies to all other minerals, survey and mining of which is much less expensive in the equatorial and tropical belts, including Africa, Australia, Southern Asia and much of South America.

Some recently published calculations by experts from the Brookings Institute are extremely revealing in this respect, according to which a one degree reduction in the so-called "per capita temperature index" (the average air temperature in the coldest month of the year in those regions where the overwhelming majority of the population and the most energy-intensive production units are located) leads to an actual drop of 1.5-2% in GDP and a 3% reduction in the economic growth rate.[6] Given that the mean temperature of the coldest month (January) in Russia is from 15 to 35° lower than in tropical countries, one can see what a heavy financial burden the notorious Russian winter places on the effectiveness of economic activity in Russia. The "cold tax" that the Russian economy pays to nature every year currently stands at around $250 bn, and was roughly three times as much in the Soviet era.

Large Distances Over Land

The large overland distances between economic actors, Russia's limited access to the main sea lanes, and the underdeveloped state of its merchant navy all have a strong negative impact on the effectiveness of the economy. Hence Russia loses out in the global economy in terms of transport costs.

Sea transport, which is much more economic than transport by land, is the principal means of carrying freight in the world economy. The carriage of freight is at least 10 to 15 times cheaper per tonne-kilometre by sea than by land. This is not just because dry cargo vessels and tankers consume much less fuel per tonne-kilometre than lorries or locomotives. Land routes – roads, railways and pipelines – require additional outlays to keep them in working order, whereas sea arteries do not. Moreover, carriage by sea avoids the need to pay duty, unlike overland transportation, which usually involves transit through several countries.

Russia transports almost all of its freight by land (mostly by rail and pipeline), and it cannot do otherwise. But in a climate of globalization the enormous overland distances significantly undermine the competitiveness of the economy, pushing up production costs, since they increase expenditure on carriage, construction of transport infrastructure, maintenance charges, and the like.

One often hears it said that Russia should take its cue from the so-called South East Asian "tigers", which have achieved development as a result of globalization. However, this prescription is clearly not applicable to Russia. The economic conditions enjoyed by these "tigers" are the converse of those in Russia and the CIS as a whole: they have a tropical climate and very small areas, and the South East Asian region itself is located at the crossing of busy sea lanes.

High Taxation

Against the background of all the above, it also has to be remembered that Russia has been compelled to maintain a high level of taxation. All the articles of budget spending in Russia – pay for public servants, upkeep of the armed forces and funding of orders for the military industrial complex (MIC) – are tens of times greater than the equivalents in many other countries.

The main reason for this is the immensely large social sector and MIC inherited by Russia from the Soviet era. The USSR had the world's most highly developed social sector, including free healthcare and free intermediate specialized and higher education. In terms of the number of hospitals, schools, colleges, universities and cultural and pre-school establishments Soviet Russia (and the other Soviet republics) was ahead of even the developed countries of the West.

Russian/Soviet citizens enjoyed one of the highest standards of social welfare in the world, and the Russian leadership is now compelled to try to maintain this, and to restore certain aspects of it in order to avoid domestic political complications. Russia is also facing the need to reform its armed forces and resolve the situation in Chechnya, and this, too, imposes an extra financial burden on the country. Where is the money to be found for re-equipping the army, training regular military personnel, conducting military exercises and maintaining a large military force in Chechnya? How are state defence orders to be funded? It all comes from the tax base – there is nowhere else. Extremely high (one might even say Draconian) taxes are essential in these conditions, under any government and any social and political system, whether democracy or totalitarianism, and this factor also makes for a lack of competitiveness of the Russian economy in the world market.

A Massive Outflow of Capital

It is the Russian economy's lack of competitiveness that has caused the massive flow of capital from the country. According to an official statement by G Gref, the Russian Federation Minister for Economic Development and Trade, the annual export of capital from Russia during the reform period (the 1990s) is assessed at \$20-25 bn.[7]

Indeed, capital flight from Russia is continuing to this day. The most conspicuous evidence of this is the "YUKOS affair". We believe that the principal reason for the arrest of Khodorkovskiy was the massive transfer of funds out of the country by YUKOS. According to some estimates, in October 2003 alone YUKOS transferred between seven and nine billion dollars offshore from Rosneft'.[8] At the same time YUKOS was in talks with the American oil firms Exxon and Chevron for the sale to them of 50% of the shares in YUKOS. Khodorkovskiy himself made no secret of his intention to "integrate" with these oil companies and even to relocate his headquarters from Moscow to London.[9]

It is thus no accident that some Russian analysts are voicing fears that the Khodorkovskiy débâcle is likely to complicate Russia's relations with the West for a long time and even act as an additional catalyst for capital flight.[10]

Unattractiveness to Investors

From what has been said above it can be seen that the Russian economy is naturally expensive. Accordingly, within a global market Russia cannot be a country where capital can be invested in the industrial or agricultural sector to greatest advantage. Massive foreign investment has therefore not flowed nor ever will flow into the Russian economy. Foreign investors realise that this immense "polar economy" is capable of "devouring" hundreds of billions of dollars without yielding any profit. As events have shown, even raw material production in Russia is of no particular interest to foreign business. All the minerals concealed in the bowels of Russia can be found in Africa, South America and Australia, where, firstly, they are present in greater quantities and, secondly, they are tens of times cheaper to recover.

More specifically, according to a number of British experts, Russian oil will be of no great significance to the world economy in the long term, since reserves are small and approaching exhaustion, and recovery is too difficult and costly.[11] A statistical report by BP assesses Russia's oil reserves at 48 bn barrels (4.8% of total world reserves) and forecasts that the "black gold" will run out by 2020.[12]

Russian experts themselves also express great concern about the depletion of Russia's oil reserves. Thus, in early April 2004 R Murzin, head of the Department of Underground Fuel and Energy Resources and Maritime Operations at the Russian Ministry of Natural Resources, officially stated that an acute crisis awaited the oil production sector of the Russian economy by 2010. He said, "Based on an analysis of oil company project documentation, the oil production plan is backed by reserves until 2010. However, proven reserves may be inadequate from, and especially after, 2010."[13]

Against this background it is significant that the OPEC countries control over 75% of world oil reserves. Saudi Arabia alone has 25.6% of world reserves (262 bn barrels). Moreover, it is estimated that it will be roughly 100 years before the reserves of the leading oil exporters (Saudi Arabia, Iraq, Kuwait, Iran, the United Arab Emirates and Venezuela) are exhausted.[14] Where, then, will lie the focus of the oil interests of the West, the industrial countries of Asia and of rapidly developing China? The answer is surely clear.

Eloquent evidence of how little attraction the real sector of the Russian economy holds for foreign investors is that, according to the Russian Federation Ministry for Economic Development and Trade, total direct German investment into the Russian economy (and Germany is Russia's biggest foreign investor) over the period from 1991 to 2001 was only around $1.5 bn, which is less than 1% of all German foreign investment,[15] and it has hardly increased in the period from 2002 to 2004.

The overwhelming majority of foreign financial inputs into Russia are not investments at all, but credits, which have to be repaid with interest and which represent a heavy burden on the economy rather than a means to growth. Extremely revealing in this connection was an official statement in early April 2004 by the Central Bank of Russia that in 2003 the country's debt to non-residents increased by 18.8%, reaching $182 bn. The Bank is very unhappy about this, as in the longer term it may pose a serious threat to the country's macroeconomic stability.[16]

This fact provides highly eloquent testimony that, despite the reduction in Russian government debt over the last two years, the indebtedness of the Russian corporate sector is growing rapidly. The whole of Russia will have to pay for it in the near future through a fall in a standard of living that was not very high to begin with.

The Energy Crisis

We can therefore assert that the principal reason for the depleted state of Russia's economy is the large-scale flow of capital out of the country, against the background of a virtual lack of major foreign investment. But this begs the question as to how Russia is still managing to keep afloat in the world market? The answer is clear: through the pitiless exploitation and underfunding of the electrical energy sector of the economy.

The state, holding a controlling interest in the "Unified Power Grids of Russia" (United Energy Systems) Joint-Stock Company, is more or less forcing the power industry to provide enterprises (for the most part, raw material producers) with virtually free electricity. Fuel and power prices in the domestic market are five to six times less than world prices, and it is this alone that maintains the competitiveness of Russian commodities, including raw materials.

The upshot of this practice is that the fixed assets of the Russian electricity holding company are extremely worn and obsolete, and they will begin to fail in the near future. The average level of wear of plant at the thermal and hydroelectric power stations which supply in the order of 73-75% and 17-18% respectively of the country's power needs, is as much as 55-60%. The situation is more favourable in the nuclear power sector, but this makes no difference to the acuteness of the problem across the sector as a whole, since nuclear stations generate no more than 7-8% of the electricity consumed by the country.

According to calculations by Russian experts themselves, if an energy crisis is to be averted in the next ten years, at least $50 bn will have to be found in order to decommission 80 GW of aged and worn-out capacity (about 50% of the total) and to commission at least 120 GW of new capacity.[17]

The Russian leadership faces a difficult dilemma. On the one hand, it is not possible to maintain low fuel and energy prices and put off tackling the problems that have accumulated in the electric power sector. On the other hand, in the absence of foreign investment, the rejuvenation of the Russian energy sector will most probably have to be funded from internal reserves, and this will inevitably drive up fuel and electricity prices. The increased cost of fuel and energy, in its turn, will automatically make Russian commodities more expensive and so reduce the efficiency of the entire economy. We believe this process will be unavoidable in the near future. Even assuming the Russian leadership tries to restrain the growth in energy prices by administrative means, it will still be useless: money will have to be found from the budget or additional taxes imposed on all the country's enterprises in order to fund the power sector.

Should energy prices in the domestic market reach the world level, it will spell the end for virtually all Russian enterprises. Even if world fuel prices remain high, fuel production will become uneconomic in Russia. Very telling in this respect was President Putin's pained reaction in October 2003 to the European Union's demand that Russian domestic fuel prices be brought into line with world prices. He said, inter alia, that "the EU will not succeed in twisting Russia's arm in its desire to achieve a sharp hike in fuel prices".[18]

The Depletion of Demographic Capabilities

The demographic crisis remains a most important negative factor as regards Russia's economic security. Whereas the population of Soviet Russia increased steadily if slowly throughout the 1970s and 1980s, a fairly intensive process of decline has been discernible since the collapse of the USSR. Russian experts themselves note that official demographic statistics substantially understate mortality in the permanent population. According to independent calculations, Russia's core population has been falling by about 1.05% or 1.12 million people a year since 1995, a rate of depopulation more than ten times higher than in Western Europe.[19]

The ageing of the Russian population also poses a major threat. Russian demographers assess that, if the current demographic trend is maintained, the numbers of pensioners and people in work will equalize, placing a heavy burden on the economy.[20]

Russia is also seeing a rapid spread of alcoholism and drug addiction among the young, further draining its labour resources. This factor has already assumed the dimensions of a threat to national security, since currently some 5 million younger people (from 15 to 40) are unemployable alcoholics or drug addicts.[21]

As a whole this section of our study has analysed the main factors affecting economic activity in Russia. It indicates that the policy of full-scale integration into the world market can only lead Russia to further economic enfeeblement. Even if, as Moscow rightly fears, Russia were to become entrenched in the role of a so-called "raw material appendage", this would only be temporary, since in the context of globalization even Russian natural resources are of no major interest to foreign business.

In view of this, Moscow will not be able to maintain its economic and social stability for long by relying solely on administrative measures and the currently favourable prices for fuel on the world market. In the very near future Russia will face the need to radically revise its former strategy of integration into the world market.

The most realistic alternative to the old strategy can only be the development of a policy of accelerated integration within the CIS, ie full-scale regionalization. In this context it is the Central Asian states, again by virtue of objective economic factors, that stand out as the most beneficial partners for Moscow in the CIS. By withdrawing from or to all intents and purposes abandoning Central Asia in the early 1990s, Moscow committed a strategic error, depriving itself of a vital economic space which, had Russia taken advantage of it, would have enabled it to greatly enhance the effectiveness of its economy.

Economic Conditions in Central Asia

It has to be noted that some of the factors underlying the fundamental non-competitiveness of the Russian economy in the world market are also characteristic of the Central Asian states. It is for this very reason that they, like Russia, have been unable to integrate effectively into the world market.

More specifically, the Central Asian countries, like Russia, inherited an enormous social sector from the USSR and have been compelled to maintain it. The result of this has been taxes at a substantially higher level than in the developing countries, and this also reduces the competitiveness of the Central Asian states in the world market. Furthermore, the Central Asian republics also lose out to coastal states in respect of a series of other economic factors (such as access to the sea), and this also impairs their investment climate.

However, overall economic conditions in the Central Asian region are a good deal better than Russia's. They ensure a higher return on investment in the real sector of the economy, thereby offering Russia a unique opportunity to solve a whole series of problems, from the modernization of its generating industry to the opening-up of the natural wealth of Siberia and the Far East. Indeed, Russian business has really no alternative for effective investment except the Central Asian region (with its favourable climate, potential resources and already developed transport network), since the transnationals have already moved in on other regions of the world that are attractive in terms of investment, and Russian companies have no hope of competing with them. We shall now consider the principal objective factors dictating Russia's interest in economic integration with Central Asia.

A More Favourable Climate

In terms of its climate the southern part of Central Asia (especially the territory south of the 43rd parallel – some of the southern oblasts (districts) of Kazakhstan, much of Uzbekistan, and all of Kyrgyzstan, Tajikistan and Turkmenistan), which falls within the dry subtropics, has definite advantages over Russia. Winter here does not last above a month to a month and a half, and is much warmer than the Russian winter. The average temperatures in the coldest month (January) vary from +1°C to +4°C, and those in the warmest month from +28°C to +32°C, with mean annual temperatures in the range from +17°C to +20°C. These temperatures are 15-20° higher than the equivalents in Russia, and this means that the profitability of any Russian production enterprise can immediately be increased several-fold without major capital investment through a big reduction in expenditure on energy and capital construction.

Lower Transport Costs

Since Central Asia is cut off from the world's sea lanes, freight here as in Russia is carried overland. There are, however, at least two circumstances which make the transport system in the southern part of Central Asia more profitable than Russia's and which hence objectively dictate Russia's interest in the region.

Firstly, all the economic actors in Central Asia are closer together than is the case in Russia. The distances separating them are measured in tens or hundreds of kilometres and not in thousands, as in Russia. This is due to the fact that a large proportion of Central Asia is desert or mountains and accordingly most built-up areas were built close to one another, at oases or in foothills.

Secondly, in the hot, dry climate of the southern Central Asia region transport infrastructure costs much less to operate than in Russia. Rail beds and road surfaces last longer, and accordingly less has to be spent on preventive maintenance and capital repairs. The cost of building transport communications is also lower than in Russia.

Moreover, Central Asia is much closer than Russia to the southern seas and therefore to one of the world's busiest crossroads for trade and economic development. Given a single "Russia - Central Asia" economic space (with no customs duty levied when crossing the borders of member states), capital investment in the south of the Central Asia region would yield much higher profits than the cold, boundless expanses of Siberia and the Far East.

Greater Attractiveness of Investment in Opening Up Mineral Resources

Russia cannot fail to be attracted by the fact that Central Asia has virtually all the natural resources that Russia has, as well as its own fuel. It would be no exaggeration to say that over half of the economically viable minerals of the former Soviet Union are concentrated in the region. Inter alia, Turkmenistan and Uzbekistan have around half of all CIS gas reserves. Recovering gas in a hot, dry climate is much easier and cheaper than in Arctic areas, and Central Asian gas will be indispensable to Russia when modernizing its generating industry.

The process of Russia's "energy return" to Central Asia has already begun, the most obvious evidence being the establishment of the so-called "Gas Alliance" between Russia, Turkmenistan, Uzbekistan and Kazakhstan, as well as the long-term strategic projects for the recovery and delivery to Russia of Turkmen and Uzbek gas.[22] Recently Russian oil companies have become increasingly involved in opening up Kazakhstan's oil reserves.

Central Asia was moreover traditionally a strategic focus for the USSR as regards non-ferrous metallurgy and is accordingly still of extreme importance to Russia for that reason. It is estimated that the total reserves of industrially important non-ferrous metals (chromium, molybdenum, tungsten, copper, lead, zinc, vanadium, aluminium, manganese, cobalt, nickel, cadmium, mercury, antimony, bismuth, tin and uranium) in the five Central Asian republics account for around 62% of the entire reserves of the former USSR and are roughly 120-150% greater than reserves in Russia.[23] And given that Central Asia has roughly a third of the population of

Russia, it can be affirmed that its per capita reserves are some six to seven times greater than Russia's.

Moreover, the cost of bringing them into production is several times less than in Russia. It is no accident that when, at the height of the Cold War, it was decided to fabricate thousands of nuclear warheads, the gigantic Navoi Mining and Metallurgical Combine and the town of Navoi were built very rapidly in Uzbekistan. It is likewise common knowledge that the Central Asia region was the main supplier of raw materials and semi-finished products for the textile industry and light industry throughout the former Soviet republics. During the Soviet era such raw materials as cotton, wool, silk and astrakhan fur were produced exclusively in Central Asia.

The Demographic Potential of Central Asia

Russia has one more interest in Central Asia. Strange though it may sound, this is harnessing the region's manpower to open up the natural resources of the Asian part of Russia.

The natural resources of Siberia and the Far East are of decisive importance to the Russian economy. The majority of the country's mineral resources and natural wealth as a whole – oil, gas, non-ferrous metals, timber, gold and other precious metals, diamonds and marine products – are all concentrated in Asian Russia. Today European Russia is poor in resources: hydrocarbon reserves in Tatarstan, Bashkortostan and the North Caucasus are depleted and the forests have largely been felled.

At present, however, Asian Russia is not only a potential source of natural wealth, but also a source of complex problems. The economy of Siberia and the Far East is in decline and their populations are rapidly migrating to European Russia. This raises the question of who there will be to exploit the wealth of Siberia and the Far East in the middle and longer terms, because young, healthy people, not pensioners and invalids, are needed for work in these harsh conditions.

Against this background, the demographic situation in the Central Asia region is more favourable than in Russia. Here the population is growing, albeit not as fast as in Soviet times, and, in contrast to the core population of Russia, the average age is very young and continuing to get younger. According to the UN, the proportion of the population under 24 years old is 57% in Uzbekistan, 61% in Tajikistan, 56% in Turkmenistan, 53% in Kyrgyzstan, and 43% in Kazakhstan, and the UN's experts say that the proportion of this age group within the population as a whole is showing a steady upward tendency. By comparison, the same age group made up not more than 32% of Russia's population at the end of 2002 and was on a downward trend.[24]

With the extremely unfavourable demographic and economic situation in Russia, the European regions are not likely to be able to open up the vast expanses of Siberia and the Far East. In this light, the countries of Central Asia offer Russia its one possible source of manpower (unless, of course, someone in Russia is intending to make, say, China a "gift" of Siberia and the Far East). Also, and of particular value to Russia, many if not most of the citizens of the Central Asian countries speak Russian and therefore (unlike with the Chinese) there would be no language barrier.

Indeed, if a viable economic union were established with Central Asia, Russia would fairly quickly – in around ten years – be able to accumulate the necessary financial resources for the full-scale opening-up of Siberia and the Far East (given that capital investment in Central Asia would be recouped rapidly because of low production costs). Russia could use these resources to fund the renewal of the industrial and electric power infrastructure in Siberia and the Far East, since it is futile to expect foreign investment in this area.

Russia would probably not be prepared to resettle workers from Central Asia in the Asian part of the country – nor would it need to: this would be too costly and problematic. Within the context of a Russian/Central Asian common market it would simply be a matter of Central Asian manpower being free to go without hindrance to Siberia and the Far East to work for limited periods.

This factor is also of great importance as regards a long-term Russian economic presence in Central Asia. If the natural wealth of Siberia and the Far East is indeed of no particular interest to the world market, then it seems clear that Moscow could make more effective use of this wealth in a Russian/Central Asian market.

Conclusion

As a whole, our study has looked at the main factors which dictate Russia's interest in Central Asia. However, it is fair to ask why these factors have not come into play before and predetermined the integration of Russia and Central Asia, and also why real integration has not occurred across the entire CIS?

The answer to this question has already been signposted in this study. It is because Russia and most of the Central Asian countries (and the CIS as a whole), caught up in the euphoria following the collapse of the USSR and the "disintegrationist" mood of the 1990s, went for a policy of full-blooded globalization, which is incompatible with effective integration in most of the post-Soviet space.

So if Russia and the Central Asian countries are less competitive in the world economy, then according to the laws of economics, capital will continue to flow to where it will yield maximum profit. And the use of capital is objectively more profitable in the world market than in most of the CIS countries, including Russia and the Central Asian states. This is why, as long as Russia and the Central Asian states maintain a high degree of openness to the world market, the depletion of their financial and other resources will continue. And this is also why it has hitherto proved impossible to find the investment not just for individual projects in the post-Soviet space, but even less so for so big a project as "integration" within the CIS.

Although some Russian politicians and public figures are still saying Russia will continue a policy of integration into the world market, objective economic factors show the opposite. The realities of life have shown that political will is not enough to compete successfully in the world market. The favourable economic conditions that Russia lacks are also essential. It is quite obvious that Russia's geography cannot be radically altered, either now or in the future. It is therefore highly probable that in the next few years Russia will face the need to choose between globalization or regionalization. Since the policy of full-blooded globalization has led Russia into the cruel grip of a crisis, we believe Moscow can have only one choice.

Two other important circumstances dictate that Russia will inevitably forge a strategic policy of regionalization in conjunction with Central Asia. Although these issues really belong to separate studies, we did not feel we could ignore them.

Firstly, Russia's gravitation towards integration with Central Asia is dictated by current trends which are leading to regionalization of the world market. Today this process is happening in America, Europe and Asia, as it leads to reduced production costs, since various obstacles to the movement of commodities and capital are partially or wholly removed in free trade areas. Moreover, it is very telling that even those countries which are, unlike Russia, winners from globalization, are pushing hard to shape regional markets. As far back as 1994 the USA set up NAFTA with Canada and Mexico. Now the Americans are directing their efforts to extending the free trade area over the entire Western hemisphere. The example of the European Union needs no commentary. It is likely that Eurozone industry will rely on the resources of the African continent. Moreover, it is also highly probable that if Russia drags its feet, some of the post-Soviet East European states such as Ukraine, Moldova and even Belarus will sooner or later join the EU.

China, likewise, is currently actively pursuing a policy of establishing a common market with the South-East Asian states, and the idea of a single currency for China and the ASEAN countries is being puffed with increasing insistence. If such a zone were established, bringing together countries with a total population of 1.7 bn, then it might possibly "swallow up" Australia too. And if Russia delays with Central Asia, that region might also be partially or wholly drawn within the orbit of Chinese economic influence.

Proceeding on the basis that the Russian economy is naturally uncompetitive, it is clear that Russia will scarcely be able to join in even any regional economic project involving the EU, ASEAN, NAFTA or the like. The only role that Russia could play in these markets is that of a supplier of raw materials and some types of arms and military equipment. Even the latter could not be kept up for long in view of the depletion we are seeing of the raw material resources and engineering base of the Soviet MIC. If, therefore, Russia does not wish to remain on the sidelines of key trends in world development, it will be compelled to follow the example of the advanced countries and build a free trade area within a common economic space in the CIS, in which the Central Asian republics will be the most valuable partners for Moscow.

Secondly, economic integration in the post-Soviet space as a whole and between Russia and Central Asia in particular is dictated by Russia's own historical experience.

According to some Russian scholars, the economic and thus the political demise of the Russian Empire in 1917 was a direct result of the policy of Nicholas II's government of integrating the country into the world economy.[25] After the Russian currency became fully convertible in 1897, with the entry into circulation of the "golden rouble" and capital enabled to move freely out of the country, events in Russia began to unfold on the same lines as in the 1990s: a mass outflow of capital ensued, resulting in the destruction of the economy and the impoverishment of the overwhelming majority of the population of Russia (and also of the minority nationality fringes of the Russia Empire). At that time the process of economic enfeeblement went on for some 20 years, so that by 1917 the country had an enormous foreign debt, an economy in tatters, and almost no gold reserves. The First World War only accelerated the process.

And if we look at the reason for the emergence of the Soviet Union in 1922 in a purely economic light, it was because after the fall of the Russian Empire Russia was of no use to anybody in the world market and had no other choice than to form a regional market under the name of the USSR. That this market took the form of a unitary communist state is a chance factor and is due to the fact that it was Communists who came to power. If, however, other political forces had come to power after 1917, they too would have inevitably set about re-establishing the common market of the former Russian Empire. This was dictated not by any ideological considerations, but by the need to survive of a Russia cut off from the world market. That the ideology and political structure of the state that was established in the process might have hypothetically been very different is quite another matter.

In the same way, if modern democratic Russia fails at the present time to take decisive steps to limit its involvement in the world market and to foster regionalization in the CIS, and above all with Central Asia, these steps will most probably be taken later, but by other forces that will come to power in Moscow against the background of an inevitable national economic crisis. These forces, however, may prove no less radical than those which created the Soviet Empire.

The authors do not believe, however, that modern Russia would reinstate the old USSR, with its inefficient, outmoded centralized distribution system. On the contrary, Moscow will most probably seek a division of labour within a common market, in which each state will earn money for itself instead of “extracting” it from central authority, as used to happen. It is true that it still hard to say exactly on what political basis the Russian/Central Asian common market will be built, but we can state with confidence that if integration were to begin today, it would be as a new Commonwealth of “Independent Capitalist Republics”, which would be fully capable of becoming an influential centre of power in the new world order that is still materializing.

ENDNOTES

1 Personal interview with director of a Russian analytical centre, Moscow, December 2003.

2 The organization, founded in 1994 as the Central Asian Economic Community, has had as its goal since then to facilitate inter-state cooperation and harmonization across both security and economic dimensions.

3 “Central Asia” here means the area of central Eurasia comprising the five states – Kazakhstan, Kyrgyzstan, Tajikistan, Turkmenistan and Uzbekistan – which were established by their declarations of independence and the collapse of the USSR in 1991. This is a somewhat notional definition, as it does not altogether take account of some geographical peculiarities or of certain demographic aspects of the situation in the region. However, it is reasonable in view of the well-known commonality of socio-political and economic development of these countries within their designated borders, the maintenance of close links between the five states and the high level of reciprocal influence they exert on each other in terms of internal and external political, economic and other processes, and their close cooperation in matters of economics, policy and, of course, security.

4 See, for example, N Ioganson, 'Resources for the 21st Century', *Itogi*, No 4 (346), Moscow, 28 January 2003, pp22-26.

5 V Filatov, 'OPEC tutelage', *Zavtra*, No 29 (452), Moscow, 2002.

6 F Hill, K Geddy, 'The Siberian cold: how Russia’s geography is slowing economic reform', *Mezhdunarodnaya Zhizn’*, No 12, 2003, pp74-88.

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[7] See Interfax interview with G Gref, 21 September 2001, http://www.news.mail.ru/news.html?81324, also http://www.dinform.ru/news/main.asp?k=112298&t=49.

[8] See, for example, S Dolgov, 'A retaliatory strike', *Argumenty i Fakty*, No 45 (1202), Moscow, 5 November 2003.

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[12] *Statistical Review of World Energy*, British Petroleum, London, June 2002, http://www.eia.doe.gov/oiaf/ieo/natgasref.html; 'Oil Reserves', *The Economist*, London, 29 June 2002, p110.

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[16] Official statement by the Central Bank of the Russian Federation. V Samedov, A Yefimov; 'Spectre of another default', *Nezavisimaya Gazeta*, Moscow, 2 April 2004.

[17] T Sabirzanov, 'Keep out, it'll kill you!', *Expert*, No 39 (346), Moscow, 21 October 2002, http://www.archive.expert.ru/expert/02/02-39-46/39 ogl.html.

[18] Quotation from K Smirnov, 'Battle at the WTO', *Kommersant-Vlast'*, No 42 (545), Moscow, 27 October 2003, pp17-18.

[19] A I Koreshkin, *Demography*, St Petersburg State Pedagogical University, St Petersburg, 2002, pp 200-202; G Kil'dishev, N Kozlova, S Anan'yev, *Population statistics and the fundamentals of demography: a handbook*, Finansy i Statistika, Moscow, 1990, p312.

[20] A I Koreshkin, op cit, p184, also interview with demographer A Vishnevskiy in the "Special Correspondent" segment of the *Vesti* TV programme, hosted by A Mamontov, RTR, 7 March 2004.

[21] Data from demographers. *Vesti za nedelyu* news and analysis programme, hosted by S Brilev, RTR, 4 April 2004.

[22] See, for example, A Grivach, 'Gazprom "digs in" in Uzbekistan', *Vremya novostey*, 15 April 2004, http://www.centasia.ru/newsA.php4?st=1082009040.

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