

# Eurasian Integration: Does Lukashenka Have a Choice?

Aliaksandr Lukashenka expressed his resentment over exemptions and restrictions in the Eurasian Economic Union treaty during a meeting with a chairman of the upper chamber of the Russian parliament on 5 May.

However, Lukashenka had effectively no other choice as to agree on the creation of this economic bloc a week earlier, because the Belarusian economy heavily depends on Russia and the benevolence of its leadership.

In the short-term, Eurasian integration and associated benefits of good relations with Russia will help to resolve [Belarus' economic problems](#), such as a high current account deficit and low international reserves.

In the long-term, however, it creates risks for Belarusian independence and its overall development. It condemns Belarus to stagnation and second-rate modernisation in the likely scenario that Russia's conflict with the EU and the US will continue for some time.

A commitment to [EU integration](#) can be more beneficial, but the government must adopt large-scale structural reforms to follow this path.

## **Exemptions Illustrate the Russian Dominance in the Union**

Leaders of the new union aim to establish a common market of 170m people based on four freedoms – the freedom of movement of persons, goods, services and capital. Armenia and Kyrgyzstan also plan to join in 2014.

At the moment, though, the union is undermined by a major exemption from the single market rules. Integrators postponed

creation of the single electrical energy market to 2019 and the single financial and oil and gas markets to 2025.

For Belarus, that means uncertainty over functioning of its [major assets](#) – oil refineries and transfer of Russian oil, gas and petroleum products to the EU. Therefore, the Belarusian president signed the Eurasian Economic Union Treaty unwillingly, bitterly opposing the exemptions.

To sweeten the pill, [Russia offered Lukashenka a \\$2bn loan](#) and the Russian state-owned bank VTB agreed to issue a \$1bn bridge loan that is supposed to reach the state's coffers in the following 14 days. Besides, Russia signed a firm agreement on the amount of Russian oil supplies to Belarus (23m tonnes in 2015 and 24m tonnes from 2016 to 2024) which can be increased if Belarus creates new oil refineries.

In addition, Russia allowed Belarus to keep \$1.5bn of Russian [oil export duties](#) in its state budget in 2015. The sides agreed on a further step-by-step reduction in the amount of duties due to be repaid to the Russian budget, with the prospect of keeping the full amount of \$3.3-4 bln at home earlier than 2025. Nevertheless, Russia wants to keep the Belarusian leadership on a short leash and exercise leverage over its reluctant partner, so this issue remains within the framework of bilateral relations.

While some commentators and members of the general public believed that Lukashenka was genuinely willing to frustrate the integration talks with Russia and Kazakhstan, he could hardly do so.

### **Lack of Viable Alternatives**

The reason for a relatively fast acceptance of integration on Russian terms lies in [the high level of dependence of the Belarusian economy on Russia](#). Close ties with Russia serve as the main pillar of Lukashenka's socio-economic model, with the total amount of Russian support in subsidies estimated at

15-16% of the Belarusian GDP.

The Belarusian economy is currently experiencing significant problems, including a high current account deficit, low international reserves and a troublesome situation in the foreign exchange market.

If Lukashenka abstains from the Eurasian integration project, Russia can quickly change its stance towards Belarus and make it comparable to the Ukrainian one, making harsh demands that would be unbearable for the weak Belarusian economy. That is the last thing the Belarusian ruler wants ahead of the upcoming presidential election.

Some Belarusian opposition parties, such as the Belarusian National Front or the Belarusian Christian Democracy, have criticised the Eurasian Union agreements, saying that they bind the country even closer to Russia. However, a strong opposition to this integration process does not exist in Belarusian society as the majority depends on the state and its paternalism.

Such opposition also does not make great sense for the economy, which remains unreformed and can quickly experience [a currency crisis similar to what happened in 2011](#) if relations with Russia worsen.

To disappointment of EU advocates in the country, the demand for redistribution of rents instead of reforms remains very high among the establishment and the population alike. However, some other aspects of Eurasian integration may encourage the Belarusian leadership to change the country's development model.

### **Eurasian Union as a Threat to Sovereignty**

Vladimir Putin is building the Eurasian Economic Union with a clear political agenda, even though his counterparts have yet to admit it publicly. As he said in his Crimea accession

speech, he wants to build and strengthen the "Russian World".

This idea is [clearly hostile to independence of Belarus](#) as a country where 70.2% of the population speaks Russian in their everyday life, according to a 2009 census. Russia dominates the Eurasian Union and will not hesitate to exercise its leverage to ensure its interests in Belarus, including the [privatisation of the most attractive assets](#) in favour of Russian businessmen.

The redistribution of oil and gas rents serves as a locomotive for integration between authoritarian leaders. They remain reluctant to take any decisive steps to put an end to their overreliance on oil revenues at the expense of their respective manufacturing sectors.

Though Belarus has a higher share of manufacturing in its GDP (25% as compared to 15% of Russia and 12% of Kazakhstan) and a lower share of fuel in its merchandise exports (38% as compared to 71% of Russia and Kazakhstan), the sustainability of the country's economy still largely depends on preferential oil agreements with Russia. In addition, if Russia continues its self-isolation from the Western world, this factor will frustrate technical modernisation and economic liberalisation.

### **EU Integration Provides More Benefits**

In the long-term, EU integration would appear to be a more beneficial option for Belarus because of the substantially larger size of the EU market. Technologically [advanced investments from EU countries](#) may facilitate the restructuring of the Belarusian economy and offset its current account deficit.

At the moment, Belarus has the lowest foreign direct investments (FDI) stock per capita (\$1,514) among all its neighbours, both in the EU and outside.



A high level of state-owned property indicates that Belarus still has a large untapped potential for the attraction of FDI. A massive influx of FDI into the countries neighbouring Belarus has been made possible due to their commitment to rigid EU accession conditions that have promoted liberalisation of trade and capital flows, as Bronk (2002) argues.

However, the Belarusian government must implement painful [structural reforms](#) to pursue this agenda. The period of Eurasian integration must be strategically used to prepare for a momentum of change in attitudes of EU citizens from the fatigue to an interest in further integration.

The Ukrainian crisis has attracted a lot of attention to the region and opened a window of opportunity that Belarus should not miss. Otherwise, Eurasian integration may preserve the nation's Soviet-like economic model and bind the country to Russia for a very long time to come.

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## **Belarus – Russia: Negotiations on Oil Donations**

On December 19 summits of the CSTO, the Eurasian Economic Community and the Customs Union will take place in Moscow. The agreement on oil supplies in 2013 is expected to be concluded during negotiations in Moscow between Lukashenko and Putin at the end of December 2012.

During last months of this year tension grows in relations between Lukashenka's regime and Russia. Lukashenka's team indicates to Moscow that it would not make concessions on issues of 'genuine integration', as it is seen by the Russian

side.

With the exception of the forced sale of Beltransgaz, major Belarusian enterprises will not be sold to Russian companies. The authorities refuse to abide by the terms of extension of the loan of the Anti-Crisis Fund of the Eurasian Economic Community.

Moscow's dissatisfaction and irritation was also manifested in the statements that supply of crude oil to Belarus would be limited by 18,000,000 tons which is by 5,000,000 less than requested by Lukashenka. Limiting supply would have considerable negative consequences for Belarusian economy which became dependent on workload of oil refineries.

### **Russia's Position**

On October 29 the Vice-Premier of Russia Adkadij Dvorkovich announced that the issue of the volume of oil export to Belarus in 2012 – 2013 will be discussed depending on the solution of the problem of solvents export to Belarus. In October, according to Russian statistics, 1 million 347 thousand tons of oil were delivered to Belarus, or 22% less than in September.

At the beginning of the negotiations (which took place in Moscow from October 31 to November 1 the Russian delegation headed by Arkady Dvorkovich announced about Russia's decision to supply 4 million tons of oil to Belarus in the last quarter of 2012, whereas the Belarusian side insisted on 5.3 million tons of oil.

As a result of the negotiations, the Belarusian and the Russian side claimed that an agreement on oil supplies for the last quarter of 2012 had been reached. However, the announced volumes of supplies were different.

The participant of the negotiations, Deputy Minister

of Energetics of Russia Pavel Fedorov said Russia would export to Belarus 4.8 million tons of oil in the last quarter of 2012, in its turn, Belarus would export to Russia 200 thousand tons of petrol.

Fedorov remarked: "Such increase in oil supplies shows our readiness to find solutions, with due consideration of long-term strategic relations with the Belarusian side." The same figures were announced by the Russian Ambassador to Belarus Alexander Surikov.

One can make a conclusion that the disagreement about the volume of oil supplies for the last quarter of 2012 has remained. Besides, disagreements on some other important issues have not been removed. There is no detailed information yet about the current suggestions from the Russian side.

The issue of compensating losses to the Russian budget from the "[solvents business](#)" has not been settled.

Just before the negotiations, the Russian side named the figure 1.5 – 2 billion USD as the tax not paid by Belarus. After the negotiations the figure rose to 2.5 billion USD. On 14 November the Minister of Energetics of Russia Alexander Novak assessed the potential losses of the Russian budget from 1.5 to 2.5 billion USD.

### **What Belarus Hopes For**

On 16 November the First Vice-Premier of Belarus Uladzimir Siamashka commented on the statements of the Russian high officials, claiming that Belarus had to fulfill the obligation to supply oil products to the Russian market. As he said, in 2012 supplies to Russia were not always profitable for Belarusian oil-refining factories.

During the negotiations Semashka strongly denied that Belarus had violated any conditions of cooperation with Russia.

The authorities take tough stance in their talks with Russia taking into account not only the context of bilateral relations. Lukashenka's team believes that Russia will make concessions and it cannot afford long term worsening of relations with its only ally.

Already now, on the eve of the last round of talks on crude oil supply, Lukashenka's team indicates to Russia how the Belarusian side will act if crude oil supply is limited. Crude oil supply from Azerbaijan will be resumed. Belarus will restrict military cooperation with Russia. It will create tension in relations within the CSTO. If Russia does not agree on Lukashenka's terms, the authorities will use other opportunities for pressure as well.

On 26 November Lukashenko repeated the main points of the Belarusian position, announced previously in the talks with the First Vice-Premier. In particular, he remarked that Belarus had not violated the terms of oil supplies in 2012. Lukashenka announced: "I think we will arrive at an agreement, there is enough oil in Russia."