

Gaidar Forum

Panel discussion "Russia and Europe: Economic Perspectives"

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Ladies and gentlemen¹,

I am glad to be at the Gaidar Forum. In times of current economic difficulties Gaidar's political legacy as a strong promoter of liberal reforms can still provide inspiration today.

As the world's largest trading block, the European Union favours economic and trade liberalism and seeks a gradual abolition of barriers to trade on a global scale. Liberalisation of exchanges with neighbouring countries, and thus with Russia, represents the European Union's interests and objectives. Yet, this policy ambition has to be checked against today's political reality.

For a number of years, the EU and Russia had assumed the existence of, what we called, a strategic partnership, based on the convergence of values, growing economic exchanges and interdependence, and a modernisation agenda for the society. We talked about the creation of a "single economic and humanitarian space from Lisbon to Vladivostok". We thought Russia and the EU could become a joint, powerful force for the good.

¹ Check against delivery

However, our differences intensified with time, particularly in relation to our common neighborhood. The illegal annexation of Crimea, followed by the destabilisation of Eastern Ukraine, eroded the foundations of our relations, have shaken the basics of European security architecture and brought into the open the differences in our worldviews. This has also been reflected in our economic relations.

In spite of the EU being Russia's largest trade and investment partner and in spite of Russia's accession to the WTO in 2012, EU operators face today increasing restrictions to export and uncertainties as regards their investments. For instance, "Buy Russian products" policies are implemented by the government and by State companies to the detriment of foreign goods, irrespective of any considerations of price or quality. Foreign investors have been forced to sell stakes in media businesses as a result of a sudden legislative change in 2014.

Those trends come at a time of economic difficulties in Russia: falling oil prices, the depreciation of the rouble, inflation and decreasing household revenues. International tensions, sanctions and countersanctions complete a landscape which has led to a sharp decline in foreign trade and investment. To mention one figure, according to data from the Central Bank, foreign direct investment into Russia in the first half of 2015 was nearly 6 times lower than in the corresponding period in 2014.

Recent developments as regards Russia's trade with Ukraine cast further doubt on the possibility to resume an ambitious plan for trade liberalisation. In spite of the EU's efforts, what remained in place of the CIS free trade regime between the two countries has been suspended on 1 January, while the trade provisions of the association agreement between the EU and Ukraine have entered into force. Furthermore, Russia has introduced

restrictions on the transit of Ukrainian goods through Russia to Kazakhstan, in spite of international principles which guarantee freedom of transit.

By making unilateral decisions, Russia, in contrast to other members of the Eurasian Economic Union, cancelled preferential trade relations with Ukraine and effectively prevented any chance for the two agreements to apply simultaneously – which is, as we know from other examples, feasible. For instance, at the present Serbia has Free Trade Agreements with the EU and with Russia. Furthermore, the European Union has Association Agreements with Israel and Egypt, with whom the Eurasian Economic Union plans to negotiate Free Trade Agreements too. A scenario of coexistence between the CIS FTA and the EU-Ukraine Association Agreement would have provided a good basis to build a positive trade agenda and a test case for gradual economic integration across the European continent.

Another field of economy where we cooperate closely is energy.

Russia remains one of the EU's major suppliers of energy products and, at the same time, the EU is by far the biggest importer of Russian oil and gas, thus contributing very significantly to the Russian budget. Over 70% of Russian energy exports go to the EU. During the last couple of years, oil imports from Russia represented around 30% of the total EU oil imports, placing Russia at the top of supply destinations. Natural gas imports from Russia to the EU remained robust in 2015, representing 41% of total imports. Although the utilisation of Nord Stream remained high, the share of Ukrainian transit increased to 47%.

This mutual energy dependence and complementarity between our economies remain important. The EU will continue to be a good and reliable customer for Russian energy. As European

businesses respect Russian rules, so should Russian energy companies, and not only, fully respect the applicable EU legislation. Any new infrastructure, including the envisaged Nord Stream 2 project, should entirely comply with the Third Energy Package as well as with the objectives of the Energy Union.

The EU is pursuing an Energy Union strategy, with a forward-looking climate policy, ensuring the diversification of supplies and routes, and integrating the energy networks, to create a fully competitive EU-wide internal energy market. Let me reiterate that the Energy Union is not directed against Gazprom or any other business entity, as sometimes we can see presented in the local media. It is aimed at better serving the European customers with greater choice, lower price and assurance of secure supplies.

Energy also has a key role to play as a confidence building measure to the resolution of the Ukraine crisis. For the foreseeable future, gas transit from Russia through Ukraine will remain very important for Europe's energy supply. Uninterrupted, stable and secure transit is also in direct interest of Russia and Gazprom – as a supplier that values its reputation for reliability. The EU will therefore continue to work with both Russia and Ukraine to ensure the flow of natural gas remains uninterrupted.

At the same time, on the international scene, the EU and Russia remain indispensable actors: we are interdependent on a wide range of bilateral and multilateral issues, be they trade, energy or global matters including migration, climate change and terrorism.

Specifically on trade, the fact is that the EU is - and is likely to continue to be - Russia's main trade and investment partner. For reference: In the 1st half of 2015, 46% of Russia's foreign trade was with the EU. For comparison: the share of the entire Asian-Pacific region (APEC) was 27%, and the Eurasian Union accounted for only 7% of Russian trade.

In view of this, we need to try to gradually repair our relations and establish a new *modus operandi* recognising our differences but seeking to work on common interests. Not a return to "business as usual", but a creation of a "new normal".

However, in order to maximise the mutual benefits that trade liberalisation and economic integration would provide it is clear that a precondition is the elimination of restrictive economic measures, linked to the crisis in eastern Ukraine. This requires the full implementation of the Minsk agreements.

Second, the EU condemns and does not recognize Russia's illegal annexation of Crimea, therefore trade with and investment in Crimea is subject to restrictions as well.

Third, the EU will continue to call upon Russia to fully comply with WTO commitments, which is a critical condition to the feasibility of further trade initiatives.

It seems difficult to reconcile a state-driven policy of import substitution with the declared goal of developing a common economic space based on free trade and open markets from Lisbon to Vladivostok. Applying discriminatory measures against foreign goods and services in government purchases or in subsidies schemes is not conducive for serious conversations on trade liberalisation and economic integration.

Fourth, the EU is following developments in the Eurasian Economic Union and maintains working contacts with the EAE Commission. We hope the Eurasian regional integration process will aim at open economic relations among the member states and towards the rest of the world.

Yet, there is a need to clarify to what extent the Eurasian Economic Union will conduct a common external trade policy and guarantee free movement of goods within its borders. As

mentioned, Russia's unilateral actions as regards Ukrainian and Moldovan goods have introduced additional exceptions to the customs union regime.

To sum up, the EU is and will remain a global player in promotion and support of international rules based system whether it concerns the human rights and freedoms, independence and territorial integrity of sovereign nations or free trade and open economies. We work with partners within the WTO as well as on regional and bilateral level who are ready in deeds and not only words to pursue an ambitious forward-looking economic agenda with less barriers and greater opportunities for trade and investment. The EU is in a free trade relationship with 88 countries in the world, and currently negotiates with major partners like the US and Japan which, in turn, also have an active FTA agenda.

Russia is the EU's third most important trade partner and it would only make sense to increase and free our economic relations. But, aside from important political considerations, the question arises whether Russia is really interested and ready to adopt a similar open and rules based approach to international economic relations as the EU is?

What we see at the moment is rather the contrary: greater political and economic insulation from the West, import substitution instead of trade liberalization and abolishment of preferential trade with such an important neighbour like Ukraine.

Ultimately, any attainable and sustainable project in our future relations must be based on an honest assessment of the readiness and willingness to envisage ambitious economic integration.

The conditions must be right: a strong commitment to economic openness; the respect of international rules; and a positive contribution to the economic and political stabilisation of our common neighbours, particularly Ukraine.

Thank you.