

Russia between integration and protectionism:
International road transport, ports, and the forestry sector

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Stockholm, Sweden
2007

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Acknowledgements

This report is based on a project commissioned by the Ministry for Foreign Affairs of Finland. Some of the issues presented here were originally discussed in late 2003 in a small seminar at the Ministry, where a paper on Finnish-Russian economic relations relating to some specific sectors was presented. Furthermore, some conceptual issues taken up briefly in this report have previously been discussed in detail in several more theoretically oriented conference papers and publications related to the project's theme.¹ The current report is a considerably updated, policy analysis oriented combination of these earlier papers, its focus – while still retaining Finnish-Russian relations and Northwest Russia as particular points of reference – being now more concerned with European Union-Russia relations as a whole. At the same time, the current publication tries to illustrate some of the challenges in respect of Russia's European relations by briefly reviewing three sectors of economic activity in Russia, namely, international road transport, ports, and forestry.

There are many people to acknowledge, though first and foremost, the author would like to thank the Ministry for its support and patience. A number of people were very kind with their time and comments, some of which have made their way into the text, these people include Harri Cavén, Harry Helenius, Hannu Kivelä, Klaus Korhonen, Seija Lainela, Antti Nissinen, Olli Perheentupa, Ilmari Susiluoto, Simon-Erik Ollus, Alexander Tashtanbekov, Tatu Torniainen, and Pertti Veijola.

The author's particular thanks go to Stanislav Tkachenko, vice rector of the St. Petersburg State University who provided, at an early phase in the project, some important information and insights in the form of a commissioned background report. The author is also grateful to Anzhelika Matveeva who helped to collect the sector-specific information used in this report, Jörg Neubauer and Patrick Lindblom who prepared the maps, Chris Smith who checked the language, and Liselott Happ-Tillberg who made the layout.

All possible mistakes and misunderstandings, as well as all interpretations, arguments and policy recommendations contained herein remain however the responsibility of the author alone.

Stockholm, April 2007

Summary

In very general terms, this report deals with the prospect of Russia becoming more closely integrated into Europe and into the world economy more generally. In a more restricted sense, it tries to illustrate some of the central issues of this theme by briefly reviewing three sectors of economic activity in Russia, namely *international road transport, ports, and forestry*. The report focuses in particular on Russian strategies, policies and decision-making in these fields, having Northwest Russia (and its borders with the EU Member States Finland and the Baltic States) as a particular point of territorial reference. (*Figure 1*) In the conclusions, the focus is placed squarely on the implications of this analysis for the whole European Union (EU), Member States and EU-based companies.

It is argued here that while Russia's declared goal is to enhance integration, at the same time its policies are clearly characterized by state-regulated protectionism. In order to understand or explain Russia's rather ambiguous behaviour along this integration *vs.* protectionism axis, two basic approaches are presented: *geopolitics* and *geoeconomics*.

The geopolitical approach calls us to imagine how Russia (or Russian leaders) attempts to hold a balance between the goals of modernization (integration as an instrument) and autonomy (protectionism as an instrument) when striving for a restoration of Russia's great power status.

The geoeconomic approach takes into account many more actors – political and bureaucratic actors, economic and financial elites, interest groups etc. From this perspective, Russia's policy towards integration results from conflicting interests, compromises, internal power relations between the elites, and different types of formal and informal influence networks, where the central actors are the state and regional political-administrative elites and the sectoral business elites.

After presenting this overall framework, the report discusses Russia's ongoing efforts in respect of closer integration with Europe and with the world economy. The focus here is on EU-Russian economic relations, particularly the so-called Common Economic Space (CES). The discussion shows that the CES is a step-by-step approach, which should, in a spirit of sectoral problem solving, bring the EU and Russia closer together. The CES seems to incorporate some elements of a free trade area, but excludes the customs union element. At the same time it retains some features of a single market, and through regulatory convergence it also includes some elements of an economic union. Ultimately however it does not fulfil the criteria of any existing form of economic integration. It is however concluded that, as a whole, this approach seems to lack a concrete vision of the future of EU-Russian relations as well as a clear-cut schedule, and thus also there is a distinct absence of any real motivation for integration.

One way to move beyond these general or abstract notions is to deal with the concrete sectors of economic activity in Russia. The three sectors reviewed, namely, international road transport, ports, and the forest industry, have been chosen because they are of particular interest from the wider perspective of developments in Northwest Russia and the EU Member States in Northern Europe. They are however very illustrative also from a more general perspective of Russian policy in respect of European integration. The respective sections outline the official Russian strategies, main challenges and tendencies, and the actor networks and decision-making practices of these economic sectors.

One can conclude that in respect of general Russian policies in these sectors, the geopolitical model is, in most cases, sufficient to explain Russia's strategic choices. Each of these sectors is from the Russian point of view strategically important economic areas, since they are related to transport, foreign trade or raw material export; thus, in the context of current Russian thinking they are closely linked to the state's national interests and security. The general goal of the Russian state is to modernise these sectors, which presupposes enhanced international cooperation and often foreign investments. At the same time, the Russian state wants to protect these economic sectors from foreign competition as much as possible and wants also to keep them in one way or another under state control. From the

geopolitical perspective, Russia's strategies in each of these fields, combining integrative and protectionist features, appear rather rational.

Nevertheless, the geoeconomic approach, focusing on conflicting interests within Russia and seeing Russia's policies more as a result of elite bargaining and compromises than of any geopolitical master plan, helps us to appreciate the complexity of concrete situations and actor networks. In this way perhaps Russia's often contradictory behaviour becomes a little more understandable.

What then would be the best strategies for the EU, its Member States and enterprises when dealing with Russia? In the concluding section of this report, it is proposed to distinguish between three levels and types of strategies, which all are simultaneously and in different combinations currently present in the EU-Russian relations. Each of the strategies could however be considerably intensified.

The first, entitled the *integration strategy*, is to be utilised at the EU-Russian level of negotiations, and would be based on the normative long-term goal of improving and deepening the EU-Russian partnership, particularly in the field of trade and economic integration. Thus, the central question here relates to going beyond the current rather vague CES-based list of priorities by making a free trade area agreement the priority goal, and after that a single market. For this, a clear-cut plan and schedule would be needed, as outlined in the conclusions. This strategy, if followed, would basically in the longer term solve most of the trade conflicts currently characteristic of EU-Russian relations.

The second, the *problem-solving strategy*, is a more short-term approach, calling for the more active defence of the EU's/Member States'/enterprises' sectoral and functional interests, to be applied in particular to problems arising from Russian protectionism, arbitrary discrimination or violation of commonly agreed norms and rules. What is needed here rather than a process of difficult asymmetrical bilateral negotiations between individual Member States and Russia, or alternatively politisized negotiations at the very top level of EU-Russian relations, is an effective EU-level problem-solving mechanism. This middle-level problem-solving mechanism, replacing bilateral or high-level political EU-Russian relations, should automatically introduce symmetrical sanctions against Russia, when Russia makes politically motivated moves in its trade policy against an individual Member State; or when its foreign trade and other bureaucracies impose such rules or sanctions on EU-based enterprises, which clearly violate previously agreed-upon rules.

The third approach, here termed the *adaptation strategy*, is best suited to the sectoral and company level. Given the problems with regard to Russia, such as protectionist legislation, companies may decide to avoid, or withdraw from, Russian markets while waiting for Russia to become more closely integrated into Europe, its norms, rules and practices. Instead, the best alternative might be just to study the current Russian circumstances as carefully as possible and then try to adapt to these circumstances.

This might include, for instance, competing with Russian enterprises with efficiency, flexibility, specialist knowledge or equipment; creating affiliated offices, registered in Russia, in order to avoid protectionism and discrimination; moving production to Russia. In the latter case, it might often be rational to try to control the whole cycle of the respective field of economic activity, thus avoiding vulnerabilities by not opting for the externalisation of parts of important elements of economic activity (as is the trend in many fields in Western company practices in countries where the market conditions function better).



Figure 1: Northwest Russia, Finland and the Baltic States

1. What explains Russia's approach to economic integration?

Integration refers to the deepening interdependence between, and the increasing coherence of, parts of a social system. Regional integration is a specific, territorially or geopolitically limited, form of integration. This kind of integration is characterised by shared formal and informal norms and rules and even supranational decision-making institutions at least in some areas of economic activity. This report focuses on EU-Russian integration in the field of *economic* activity, and especially Russia's policies in this field.

It will become clear in the context of this report that Russia's policies towards Europe appear rather paradoxical. Russia's declared goal is to be more closely integrated into Europe, thus – from a mainstream European perspective – presupposing market opening and liberalization, common norms and rules. But at the same time Russia's strategies, policies and decision-making structures are clearly characterized by state-regulated protectionism and fear of losing its decision-making autonomy and sovereignty.

Why this ambiguity? Should we try to understand or explain Russia's behaviour along this integration *vs.* protectionism axis; two basic explanatory approaches² can be highlighted, namely, geopolitics and geoeconomics.

The geopolitical approach calls us to imagine how Russia (or Russia's leaders) balance between the goals of modernization (integration as an instrument) and autonomy (protectionism as an instrument), when striving for the restoration of Russia's great power status in rather traditional spirit. The geoeconomic approach will take many more actors into account – political and bureaucratic actors, economic and financial elites, interest groups etc. From this perspective, Russia's policy towards integration results from compromises, conflicting interests, and different types of formal and informal influence networks, where the central actors are the state and regional political-administrative elites and the sectoral business elites.

Geopolitics: restoring Russia's great power status

Should we look at Russia's policies towards integration from the perspective of geopolitics³, Russia's behaviour is guided by the general goal of restoring her great power status. Economic policy and resources are seen as one of the main elements of this desired status.

One can derive two conclusions from this basic idea. First, Russia has to modernize itself if it wants to increase its economic capacity and through that, its overall power. Modernization in the contemporary global context presupposes closer integration with Europe and with the world economy as Russia currently plays only a marginal role in the global economy and particularly so in the area of technological development. The positive correlation between successful modernization and integration is generally accepted in Russia, at least by the current political elite. Integration is seen as the only way to receive the necessary capital (investments, loans) for modernization, to enable the transfer of the technical know-how to Russia, and to effectively facilitate Russia's export and import.

On the other hand, attempting to reclaim its great power status in a traditional sense presupposes the preservation of a certain degree of self-sufficiency and for the state apparatus the securing of its decision-making autonomy and sovereignty. This is also the case in the economic field, and particularly so in the fields, which Russia has defined as "strategic" from the perspective of economic and military security, such as energy, raw materials and other main export products as well as that of transport infrastructures.

Privatisation has been allowed in most economic areas within the framework of the Russian market economy. However, the Russian state has to be able to retain control over the key areas. For this reason these “sensitive” fields remain difficult to open up to far reaching liberalization or foreign ownership such that the strategic level of decision-making would move beyond the reach of the Russian state.⁴ By the same token, no supranational models of economic integration, limiting Russia’s decision-making autonomy, are deemed acceptable.

In this approach Russia differs from the “European model”. It has been argued by some analysts that Russia seems to base its thinking on the concepts of states and sovereignty, while Europe, including European great powers, base their rather on the concepts of societies and integration, including far-reaching adaptation to common norms and rules and the respective supranational decision-making institutions. In this context, Russia is accepted as a great power by others, but it is a “player of different kind”.⁵

To put it slightly differently, the combination of the two goals, modernization relying on Western investments and technology while preserving as much autonomy and sovereignty in terms of state power as possible, can be interpreted as a contemporary reflection of the eternal Russian solution to the question as to how Russia should be develop. In the same way, capitalism originally came to the Czarist Russia based on Western investments and technology, accepted as a necessary tool of modernization against the pressure of the Western world, while the political and economic systems were submitted to the state’s great power interests.

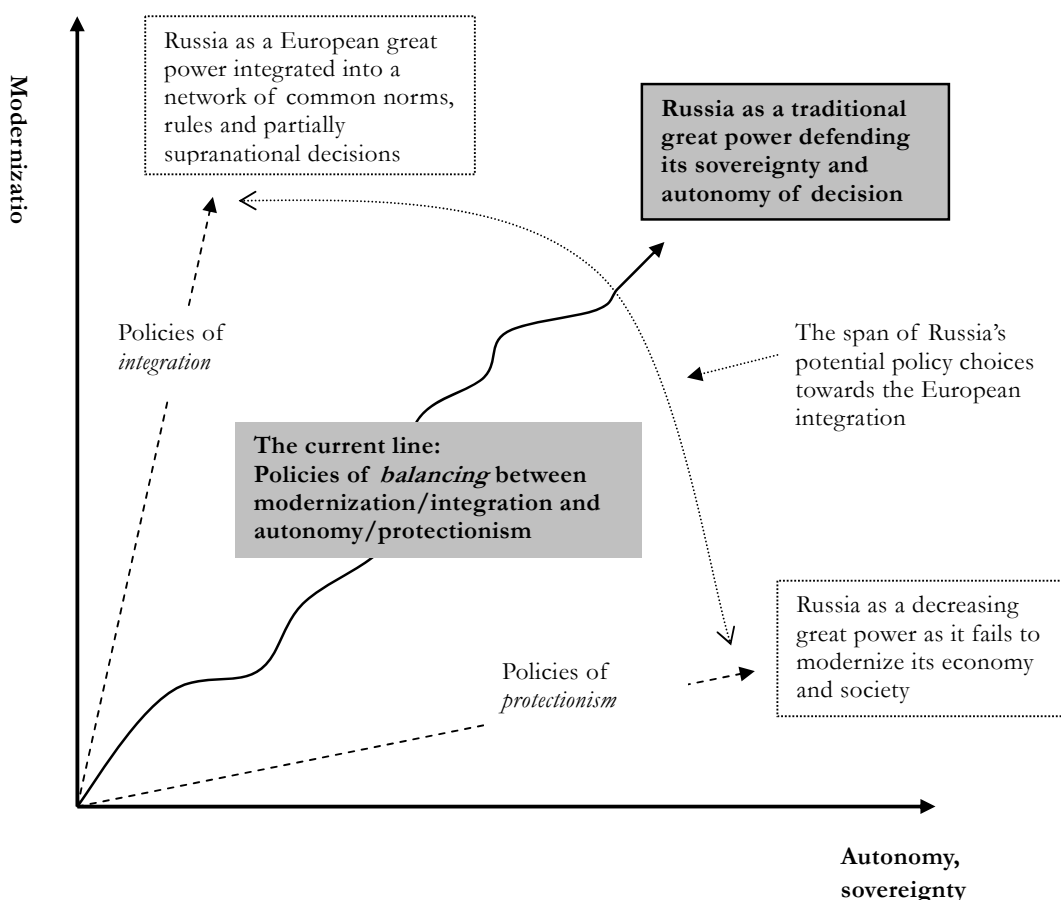


Figure 2: Geopolitics: Russia balancing between modernization and autonomy

As is illustrated in *Figure 2*, this same logic explains why Russia has adopted a strategy which aims at integration as a basis for modernization but at the same time relies on protectionism as a tool for preserving and exercising autonomy and sovereignty. Looking at

the issue from this perspective, most of Russia's practical policies and decisions become more understandable, as Russia seeks a balance between these two overarching goals.

Geeconomics: conflicting elite interests

Geeconomics refers to the idea that Russia's approach towards integration cannot only be explained within the context of a unitary state's geopolitical interests but rather that we have also to look in greater detail at its economic structure and the respective interests. If we start by looking at the foreign trade structure of Russia (see *Figure 3*), it is obvious that oil, gas and low value metal products constitute an overwhelming proportion of Russian exports, while Russia imports capital and finished goods such as machinery, equipment, chemicals, consumer goods and food.⁶

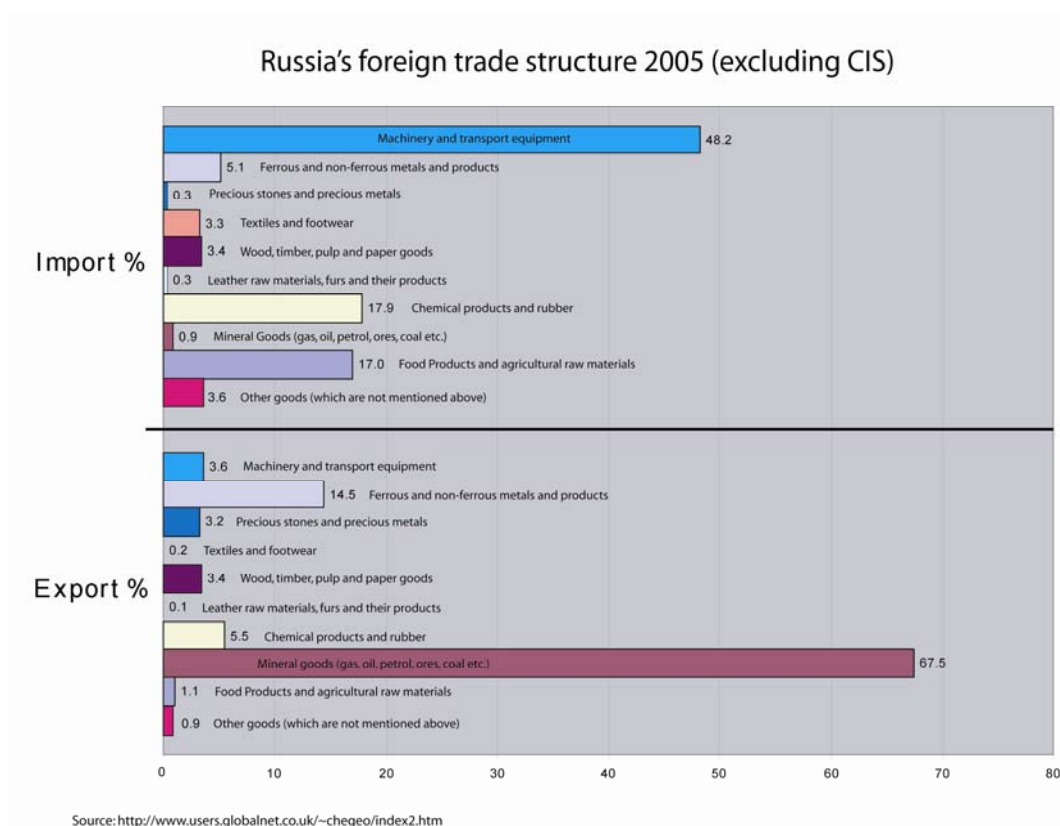


Figure 3: Russia's foreign trade structure 2005 (excluding CIS)

It is, however, hard to make any general conclusions on this basis alone, except that it seems natural that the Russian state's self-interest calls for efforts in respect of diversification and the balancing of its foreign trade structure such that Russia will not remain simply a raw material and energy producer for the rest of the world, heavily reliant on outside technology. Different parts of the Russian economy however may have contradictory interests *vis-à-vis* integration

From this perspective, the role of the Russian business elites becomes important. The role, nature, and influence of the Russian business elites, the so-called *oligarchs* or financial-industrial groupings, is a much discussed theme. At minimum they are viewed as an essential part of the actor network relating to Russia's modernization strategy, though currently their direct influence on state policy is rather limited as compared to that of the 1990s. This is so, because an important tendency in recent years' Russian policy has been that while the business elites, or the oligarchs, earlier were actively involved in high-level political decision-making, today the political elite is more and more involved in the business elites' decision-

making. This development has sometimes been described as a change from “oligarchic capitalism” towards “bureaucratic capitalism”.

In any case, in this kind of a system, the interests of Russia and the so-called “rules of the game” in the economic field do not emerge from any unambiguous geopolitical state interest but from within the network of partially conflicting interests defined by the various levels of the Russian state bureaucracies and the Russian business elites. The policies of integration and protectionism arise from the results of this interaction process.

This approach takes an alternative view compared to the most economic theories of integration, which are based on classical liberal economic theory emphasizing the general benefits of free markets as the result of integration. According to classical liberalism, integration, at the macro level, is supposed to enable the optimal international division of labour and through that optimal economic growth, equal rights in economic activity, a more even income distribution, and increasing freedom of choice.⁷ The geoeconomic perspective, however, relies more on approaches, where integration is looked at from the perspective of a *conflict*.

Some analysts within these approaches⁸ put emphasis on inter-elite rivalries as the central conflict behind the integrative developments. It is a question of redistribution of capitalist space. Here we can differ between two tendencies. On the one hand, European integration can be interpreted as rivalries between the United States’ and European capitalist classes. European integration thus would be caused by the pressure from American capital, being a defensive reaction of European capital. On the other hand, some analysts emphasize the fragmentation of the European capitalist class, especially the conflict between the national and transnational economic elite interests. National political elite protecting national economic elites favour protectionism, and those economic elites and their political allies who have transnational interests favour free trade. This rivalry is then mirrored in the policies of nation states towards integration.

This analysis can easily be applied to Russia’s relations towards European integration. In other words, this approach suggests that European integration (regional trade arrangements, custom unions etc.) has great redistributive consequences, creating both winners and losers within the participants themselves. It is generally regarded that the majority of Russian business elites has a positive attitude to deeper integration with the European and world economies and consequently do not categorically oppose the liberalisation of foreign economic relations and domestic markets. The benefits of integration would be growing export markets, simplified importing, growing foreign investments, greater possibilities to receive foreign loans and the transfer of technical know-how to Russia.

However, in some sectors integration is seen as a threat rather than a possibility, since these sectors do not have a realistic potential of penetrating European markets (for economic, political or quality-related reasons). These sectors thus concentrate on domestic markets and support protectionism.⁹

Parts of the Russian business sectors (or capitalist class) are not only looking at the benefits of integration for Russian-based industries, but are actively seeking for transnationalisation of Russian capital, especially in the form of foreign direct investments (FDI). Gas, oil, metallurgy companies and maritime transportation make the major part of this transnationalisation. Territorially, about a half of Russian FDI is in the enlarged EU and a quarter in the USA; the three main individual countries are the USA, Poland and Germany, making over a half of all FDI. While the big Russian companies often are state-controlled companies, meaning that their foreign trade strategies are intermingled with Russian foreign policy in one way or other, there are also growing amount of free marketers led by economic rationality in their foreign operations. However, also the natural resource-based companies are seeking for markets and efficiency, and the EU markets are often prioritised because of the superior profits compared, for instance, to the Commonwealth of the Independent States (CIS).¹⁰

Thus, the different Russian business elites do not have identical interests. Preferences between and within the elites vary, or may be contradictory. Moreover, different business elites do not have equal lobbying capacities and access to political decision making.

Russia's negotiations with the World Trade Organization (WTO) provide evidence of how difficult it sometimes is to combine the general will of integration with the multiple and contradictory interests of concrete economic sectors. It can well be assumed that closer integration with the EU will bring even bigger problems. In other words, EU-Russian integration will create winners and losers in the Russian economy. This will have an affect not only on the different sectors of the economy but also on Russia's regions¹¹. (The same goes for the EU; for instance, the EU textile industry and metallurgy sectors are often lobbying for protectionism against imports from Russia.)

To sum up, one can conclude that when the interest groups supporting integration have more influence than those that oppose integration, the integration process at large will proceed. The normative lesson from this perspective is that should one want EU-Russian integration to proceed, one should seek to buttress those economic and political elites that see their self-interest as being connected to further integration. From an analytical point of view, this notion may be used in understanding the process of integration – both successes and failures – between Russia and the EU. We should carefully consider the respective sector's internal elite power structure, interests and estimate the sectoral elite's influence on the decisions taken in the Russian federal, regional and local decision-making environments.

From this perspective, Russia's political and administrative decisions are not a result of any geopolitical master plan, but rather that of compromises, conflicting interests, and different types of formal and informal influence networks, where the central actors are the central state apparatus, regional political-administrative elites, and the sectoral business elites. This decision-making complex is also to a varying extent influenced by external actors and factors, such as other countries, international organizations, international business corporations, the Russian media and civil society. This framework of analysis is summarized in *Figure 4*.

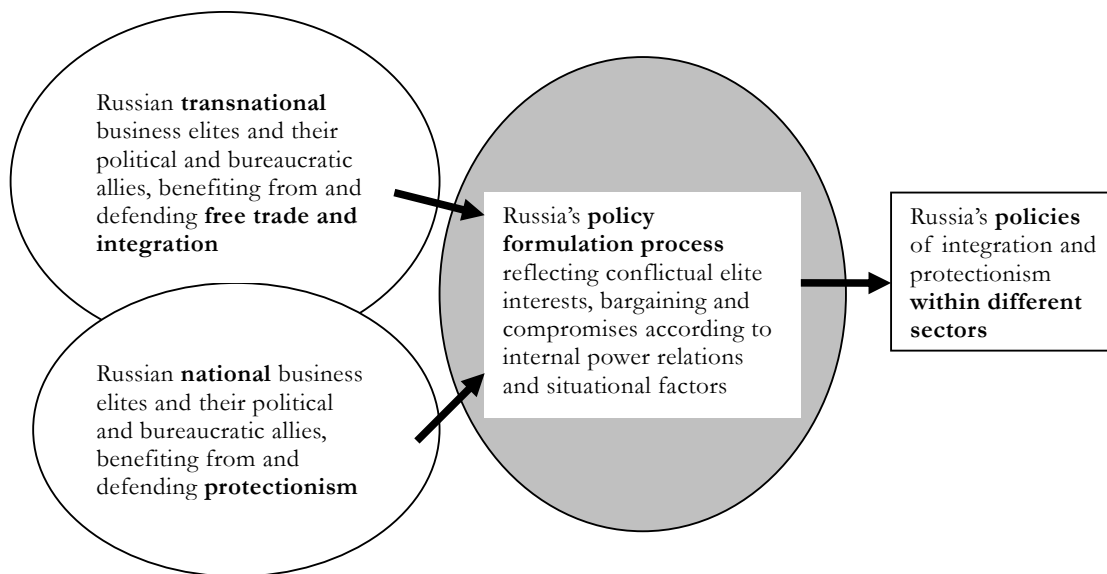


Figure 4: Geoeconomics: Russia's policies as a result of internal bargaining

2. The growth of the pragmatic line

The most topical issue in respect of Russia's integration into world economy is her forthcoming but considerably delayed entry into the World Trade Organization (WTO). This section begins with a brief discussion of this issue. The bulk of the section however focuses on the so-called Common Economic Space (CES) which is supposed to be established between Russia and the EU.

Russia and the WTO: searching for the "best balance"¹²

Russia originally applied for membership of the WTO's predecessor, General Agreement on Tariffs and Trade (GATT) in 1993, while negotiations with the WTO finally began in 1995. Obtaining membership has however proved to be rather more complicated than was originally thought in the initial spirit of euphoria generated by the desire to "join the West".¹³

In practice the process has taken place in terms of "rounds" through the preparation of newly updated reports on Russia's membership conditions. Since Russia has had to agree with each of the member states individually a period of rather arduous bilateral bargaining has had to take place alongside the multilateral agreement track.

In the years since the end of communism Russia's self-confidence has increased with the realisation of its growing economic power to the extent that now it no longer merely wants just to join the WTO but rather it is seeking to join with certain conditions attached.

Although the WTO accession was defined as a "top priority" by President Vladimir Putin himself when he started his first term in 2000, and Russia consequently became much more active in this field, it has been noted that the "increased attention to negotiations, instead of leading to greater openness, has resulted in protectionism on the part of the Russian government [...] Whereas Russia previously pursued accession as a top priority and seemed willing to accept attendant sacrifices, it now demands clearly defined terms and desires accession less urgently."¹⁴ Others have noted that this more reluctant attitude was partially a reaction to the delay of the WTO accession. From 2000 to 2003 Putin made Russia's WTO accession "one of his key priorities, but after he failed to reach his self-imposed deadline of 2003, his interest wavered".¹⁵ In any case, the next quotation crystallizes the official Russian approach excellently:

"The objective of the accession negotiations is to achieve the most favourable conditions for Russia joining the WTO, i.e. the best balance possible between the benefits of accession and the concessions in forms of tariff reductions and domestic market opening. [...] the balance of rights and obligations of Russia during its accession to the WTO should contribute to its economic growth and not *vice versa*."¹⁶

It seems clear that WTO accession creates winners and losers in Russian economy, and therefore interest groups lobbying for and against the WTO have emerged in Russia. Some analysts have noted that President Putin has during his second period joined those who criticize market liberalism and instead has adopted, at least at the rhetorical level, a policy of "unlimited state intervention, industrial policy, and protectionism".¹⁷

In any case, Russia's WTO accession seems to be an ever-delaying issue. As for today (April 2007), there are still some unsolved questions between Russia and WTO on multilateral level, such as immaterial copy rights and agriculture.

In bilateral negotiations, Russia and the USA still negotiate about the abolishment of the so-called Jackson-Vanik amendment with regard to Russia, a politically motivated Cold War era US trade policy instrument. Also Georgia and Moldova, both motivated by political

disagreements with Russia, have been putting on the brake for Russia's efforts to join the WTO.

The EU and Russia agreed on their bilateral issues concerning Russia's WTO accession in 2004. In practice, it can be argued that the EU traded its support by linking it to other issues, such as Russia's ratification of the greenhouse gas related Kyoto protocol as well as Russia's acceptance of the trade policy consequences of the EU enlargement vis-à-vis the new Member States. There have, however, emerged new problems between the EU and Russia, as the EU has criticized Russia not following the 2004 agreement. The current main issues deal with the increase of customs duties in round wood export, Russia's boycott against meat import from Poland and the double tariffs of Russian railways.

In some occasions, the EU has more or less directly claimed that Russia politicizes trade and uses it "as a political commodity", and the EU sees that the WTO can be used to avoid these types of disputes.¹⁸

The limits of EU-Russian integration

In the development of EU-Russian relations the same tendency towards pragmatism is visible. In principle the goal is closer EU-Russian integration. In practice however Russia is often simply unwilling to accept the consequences of integration, that is, market opening and the harmonization of rules never mind supranational regulation. While both sides are committed to the objective of closer cooperation and speak about integration as the goal, pragmatism and self-interest seem to be the main ideology characterizing their relationship.

"Everything but institutions"

One might note that the spirit was perhaps more optimistic, even utopian, in terms of Russia's integration into the EU in the immediate aftermath of the collapse of the Soviet Union and the establishment of the Russian Federation. In the course of the early and mid-1990s, President Boris Yeltsin and Prime Minister Viktor Chernomyrdin used to make occasional but repeated pronouncements on the possibility of Russia's EU membership in the long term. Today, while almost all the other European countries have joined or are striving to join the EU, Russian membership is now considered both impractical and undesirable.

In the EU the idea of Russian membership was always questioned. Even where all possible formal criteria and the full body of the *acquis communautaire* were to be met, the underlying thinking often is that Russia is simply too vast in terms of territory and population, and militarily too independent and important a global actor, to join the club: as such, Russia's membership would alter the whole balance and nature of the EU.

While this attitude was initially often seen negatively in Moscow, as one that discriminated against Russia, Russian politicians no longer speak of membership as a realistic or even desirable goal. The change towards more pragmatic and self-confident line vis-à-vis the EU took place in late 1990s. Consequently, as stated in *The Russian Federation Middle Term Strategy Toward the European Union (2000 - 2010)*¹⁹ published in 1999, relations between the EU and Russia should be based on the "objective need to establish a multi-polar world", with Russia being one of the "poles":

"During the period under review, partnership between Russia and the European Union will be based on the treaty relations, i.e. without an officially stated objective of Russia's accession to or 'association' with the EU. As a world power situated on two continents, Russia should retain its freedom to determine and implement its own domestic and foreign policies, using the status and advantages of a Euro-Asian state and as the largest country of the CIS, independence of its position and activities at international organizations."

While the Russian idea of a multi-polar world has always included understanding also the EU as a "pole", potentially balancing together with Russia and other great powers the hegemony

of the United States, President Putin chose to underline exactly this perspective in his article celebrating the 50th anniversary of the European Union, widely published in Russian and European media in March 2007. In this article, Putin also repeated the 1999 policy line towards the EU:

“We view European integration as an objective process, representing an integral part of the emerging multi-polar world order. [...] The development of multifaceted ties with the EU is Russia’s principled choice. It is true that in the foreseeable future, for obvious reasons, we have no intention of either joining the EU or establishing any form of institutional association with it. Viewing the situation in a realistic light, Russia intends to build its relations with the EU on the basis of a treaty and a strategic partnership. In this regard I agree with Romano Prodi’s formula of our relationship with the EU: ‘Everything but institutions’.”²⁰

Thus, the Russian leadership has explicitly chosen to see the world through the traditional great power perspective, which virtually excludes the option of Russia’s EU membership and also any other forms of supranational governance in the key areas of state policy.

What is a Common Economic Space?

As the membership option is excluded, the current solution to the continuing need for closer EU-Russia cooperation is that the EU and Russia should create “common spaces” in four areas of cooperation: The Common (European) Economic Space (earlier CEES, now CES), the Common Space of Freedom, Security and Justice, the Common Space of Cooperation in the Field of External Security, and the Common Space of Research and Education, including Culture. (For a summary of the Four Common Spaces, see [Table 1](#))²¹

From the economic integrationist point of view, generally regarded as reflecting the core motor of integration, the CES in particular raises a number of interesting issues. The idea for CES emerged rather surprisingly at the EU-Russia Summit in May 2001.²² This activity resulted in *The Common European Economic Space (CEES) Concept Paper*²³ in 2003. The *Concept Paper* defines the CEES as follows:

“The CEES means an open and integrated market between the EU and Russia, based on the implementation of common or compatible rules and regulations, including compatible administrative practices, as a basis for synergies and economies of scale associated with a higher degree of competition in bigger markets. It shall ultimately cover substantially all sectors of the economy.”

The basic instruments of this concept are “market opening”, “regulatory convergence” and “trade facilitation”. In May 2005 the EU and Russia agreed upon the *Road Maps* for the above-mentioned four Common Spaces, this document altogether ran to 52 pages with a list of priorities and short action plans, including a *Road Map* for the CES (See [Table 2](#)).

What then is the goal of the CES, what is “an open and integrated market”? Indeed, several types and degrees of economic integration exist some of which entail little more than extended cooperation in trade terms while others envisage far deeper political and economic commitments. Following the classical categorisation²⁴ based on the ideal of maximal liberalisation and convergence, we can distinguish between five different types of economic integration: free trade area, customs union, single market, economic union and full economic integration.

Let us consider the CES concept in light of the above-mentioned categories or degrees of integration. What kind of a relationship does it indicate between the EU and Russia? (For a summary of the below review, see [Table 3](#))

Table 1 Summary of the Four Common Spaces²⁵	
The Four Common Spaces	Priorities
Common Economic Space	- General issues of trade and economic cooperation - Trade facilitation and Customs - Networks: telecommunication and transport - Energy - Space - Environment For a more detailed summary, see Table 2
Common Space of Freedom, Security and Justice	Freedom - The movement of persons - Border issues - Migration policy - Asylum policy
	Security - Terrorism - Falsified documents - Transnational organised crime - Anti-money laundering regime - Narcotic drug problem - Trafficking in human beings - Corruption - Trafficking in stolen vehicles and items of cultural and historical value
	Justice - Efficiency of the judicial system - Cooperation on criminal matters - Cooperation on civil matters
Common Space of External security	- Strengthened cooperation and dialogue on the international scene - Fight against terrorism - Non-proliferation of the weapons of mass destruction - Cooperation in crisis management - Cooperation in the field of civil protection
Common Space of Research and Education, including Cultural Aspects	Research, science and technology , aiming at - Structuring a knowledge-based society in the EU and Russia - Promoting competitiveness and economic growth - Enhancing the link between research and innovation - Maintaining small and medium size entrepreneurship in the field of research and innovation
	Education - Adopting higher-education comparable curricula and degrees (the so-called Bologna process) - Promoting academic mobility - Promoting life-long learning - Increasing the attractiveness of the Higher education systems of the EU and Russia
	Culture - Promoting cultural cooperation and exchange - Promoting cooperation of the cultural industries - Strengthening the European identity “without dividing lines”

Table 2 Summary of the Common Economic Space²⁶		
Main issues of cooperation	Sub-issues of cooperation	Objectives
General issues of trade and economic cooperation	Regulatory Dialogue on industrial products, especially in: ICT, Radio and Telecommunication Equipment Electrical Equipment and Machinery Medical Devices Automotive industry Textiles Pharmaceuticals Forest-based and related industries	Harmonized and compatible standards, regulations and conformity assessment procedures
	Public procurement	Transparent, competition-based systems of public procurement
	Intellectual, industrial and commercial property rights	Improvement of the legislative and law enforcement systems in order to enhance competitiveness and improving investment climate
	Competition	Approximation of competition legislation and strengthening of implementing of competition policy
	Investment	Improving investment climate, transparency, predictability and simplification of regulation
	Enterprise policy and economic dialogue	In-depth dialogue on economic reform and enterprise policy, especially in: Automotive industry Textile industry Mining and metallurgical complex Chemical industry Aerospace industries
	Interregional and cross-border cooperation	Deepening and diversification of interregional cooperation
	Financial services (banking, insurance, securities)	Stability and sound financial system, protection of financial services consumers
	Accounting/auditing and statistics	Transparency, share-holder protection, creating favorable investment conditions
	Agriculture, forestry, timber, fisheries. Sanitary and phyto-sanitary measures	Regulatory convergence
Trade facilitation and Customs		To facilitate, to standardize and to automate external trade operations
Networks: telecommunication and transport	Telecommunications, information society and e-business	EU-Russia Information Society area
	Transport	The complementarity of the Russian and EU transport sectors and gradual integration of transport networks
Energy		Intensifying the EU-Russia Energy Dialogue, especially in sustainability, reliability, distribution, transportation, energy efficiency, energy savings and renewable energies
Space		Effective EU-Russia cooperation
Environment		Promoting the commitment to and implementation of international environmental agreements

Table 3 The degree of economic integration in EU-Russian relations		
Degree of integration	Description	Relevance for EU-Russian economic relations
Free Trade Area (FTA)	A group of countries that have agreed to eliminate tariffs, quotas and preferences on most goods between them.	<i>Unclear, but probably the most logical solution.</i> FTA is mentioned in the PCA (1997) as a possible future subject of negotiations, if the circumstances will allow it. FTA is also mentioned in the EU strategy on Russia (1999) and Russian strategy on the EU (1999) as a future goal. Not mentioned explicitly in the CEES <i>Concept Paper</i> (2003) or the CES <i>Road Map</i> (2005). Some signs of a renewed interest from the EU in speaking about the FTA from 2006 onwards.
Customs union	A FTA with a common external tariff; the members of a customs union have the same policies and common rules (customs duties, quotas, preferences and so forth to all goods entering the area) with respect to non-members.	<i>Problematic, not in sight.</i> The CEES <i>Concept Paper</i> (2003) or CES <i>Road Map</i> (2005) does not mention the prospect of a customs union. Problematic from the perspective of the customs union plans of Russia with Belarus, Kazakhstan and the Ukraine, which might not be compatible with EU-Russian customs union perspectives.
Single market	A customs union, buttressed with common policies on product regulation, and freedom of movement of all the factors of production, that is, goods, services, capital and labour.	<i>Unclear, possible, but not in its traditional form.</i> There are elements of a single market in the CEES <i>Concept Paper</i> (2003) and the CES <i>Road Map</i> (2005), even if the very term is not used. The problem is that the traditional definition of a single market also includes a customs union.
Economic union	Everything above combined with the harmonisation of national economic policy norms, rules and regulations, with supranational instruments and decision-making under legal obligation.	<i>No practical relevance.</i> While there exist some signs of regulatory harmonisation, there are no signs whatsoever that the EU or Russia would be willing to lead the CES process as far as the creation of supranational bodies to govern common economic policies.
Full economic integration	Everything above combined with supranational governance of different sectors of economic policy	
Monetary union	Common currency and monetary policy	

The Common Economic Space as a free trade area?

A *free trade area* (FTA) refers to a group of countries that have agreed to eliminate tariffs, quotas and preferences on most goods between its members. Typical FTAs include, for instance, the European Free Trade Association (EFTA) and the North-American Free Trade Agreement (NAFTA).

As a matter of fact, the original idea in this context was specifically to create a FTA between the EU and Russia. The idea emerged from the Russian side during the *Partnership and Cooperation Agreement* (PCA)²⁷ negotiations at the beginning of the 1990s, which continues to form the main legal framework for EU-Russian cooperation. Russia did not however attain its original objective, which was that the PCA would define the date to begin negotiations on a FTA between the EU and Russia. However, an article (article 3) was added to the PCA, which stipulated that the “parties shall examine together in 1998 whether circumstances allow for the beginning of negotiations on the establishment of a free trade area”. In January 1998, when the parties met for the first time after ratification of the PCA, it was jointly concluded that a FTA was not timely.

The goal of a FTA was however also included in the EU documents and strategies drafted after the PCA. Thus, in the *EU's Common Strategy Towards The Russian Federation*²⁸ (published in 1999) the Union announced that it “will also examine how to create the necessary conditions, in addition to World Trade Organization accession, for the future establishment of an EU-Russia Free Trade Area”. In the strategy, this question is connected to Russia's WTO membership, the development of Russia's own legislation and standards according to the PCA, i.e. harmonisation with EU legislation, and also more indirectly to the development and stabilisation of democracy and the rule of law in Russia. *The Russian Federation Middle Term Strategy Towards The European Union (2000 - 2010)*²⁹, which Russia in 1999 prepared as an answer to the EU's strategy, is also based on the future prospect of the “creation of the Russia-European Union free trade zone”.

After the initial impact of these documents ran its course, the FTA goal was subsequently to be overshadowed by Russia's efforts in respect of securing WTO membership, and, apparently, was finally removed from the active agenda for that reason.

Is the CES supposed to become or include a FTA? In fact, while the *Concept Paper* from 2003 notes that the CES’ “scope shall be broader and deeper in comparison to the WTO and PCA provisions”, it does not include the term FTA. Instead the *Concept Paper* refers to “eliminating obstacles and creating opportunities” in four areas of economic activity, namely the “cross-border trade of goods”, the “cross-border trade in services”, the “establishment and operation of companies” and “related aspects of movement of persons”. The *Road Map* from 2005 to some extent details these overall goals, but it does not mention the FTA.³⁰

Thus, relying on official CES documents thus far, it seems clear that the CES should be something like the PCA+ and WTO+ yet it remains unclear as to whether it is, at the same time, supposed to be, so to speak, FTA-, FTA or FTA+.³¹

During 2006 however, the European Commission again in several occasions signalled the prospect of a free trade area with Russia as part of the preamble to the talks on future EU-Russia cooperation. In fact, the EU's *Country Strategy Paper 2007-2013, Russian Federation* first time makes the connection between the CES and a free trade area by stating that “the gradual establishment of the Common Economic Space should bring closer the ultimate goal of a free trade area.”³²

It is probable moreover that the FTA goal will again be mentioned in the renewed PCA to be negotiated between the partners before the current agreement ends in 2007. In any case, one can say that at the declaratory level both parties are loosely committed to the future of the FTA, although its immediate realisation has not been particularly realistic in the short run.

Or a “single market without a customs union”?

A *customs union* in turn is a FTA with a common external tariff, that is to say, the members of a customs union use the same policies and common rules (customs duties, quotas, preferences and so forth on all goods entering the area) with respect to non-members.

Examples of customs unions include the European Community/Union, the EU-Turkey Customs Union and the Southern African Customs Union, for instance.

Neither the *Concept Paper* nor the *Road Map* mentions the prospect of a customs union. In contrast, while the customs union issue seems not to be on the agenda at least for the time being between the EU and Russia, this has been one of the main issues between Russia and some of the former Soviet republics. Among the many partially overlapping economic integration efforts in the post-Soviet space, the most far-reaching development concerns the Single Economic Space (SES) between Belarus, Kazakhstan, Russia and Ukraine.³³ This indicates that Russia is aiming at a much closer level of integration with these countries than it hopes to attain in respect of EU-Russia integration. These agreements are however written in the spirit of a “step-by-step” arrangement and thus full implementation of the customs union or even of a FTA between the countries remains a distant prospect.

Whatever the future result, in respect of the impact of these arrangements on the EU-Russia CES, it remains unclear as to how the SES or any other form of CIS economic integration and EU-Russian economic integration should be combined, and how the elements of a customs union would fit the concept. In many ways, Russia is trapped between the CIS/SES and EU-Russian integration, the forms and goals of which are not readily compatible.

A *single market* is traditionally defined as a customs union, buttressed by common policies on product regulation, and the freedom of movement for all the factors of production, that is, goods, services, capital and labour. Examples of single markets include the European Community and the European Economic Area (EEA).

Elements of a single market clearly emerge from within the *Concept Paper* and the *Road Map*, even if the actual term is not explicitly used. Instead, both the *Concept Paper* and the *Road Map* speak about an “open and integrated market between the EU and Russia”. Furthermore, there is talk of removing most obstacles to the free movement of goods, services, capital (and labour³⁴). Without being a customs union, however, the CES would not follow the traditional definition of a single market.

As a very developed form of economic integration, an *economic union* means everything specified above combined with the harmonisation of national economic policy norms, rules and regulations, basically with supranational instruments and decision-making under legal obligation. Should one combine it with the supranational governance of different sectors of economic policy, this union would reach the stage of *full* economic integration. A tighter definition adds to this the establishment of a monetary union, with a common currency and monetary policy. The euro-zone within the EU fulfils these criteria.

There are however no signs whatsoever that the EU or Russia would be willing to lead the CES process as far as the creation of supranational bodies to govern common economic policies.

Legal harmonization as an integration tool?

While an economic union with supranational bodies seems not to be the goal of the EU-Russia relations, harmonization or approximation of relevant Russian legislation with that of the EU is nevertheless required also for the FTA and single market approaches.

In principle, this approach is included in the official EU-Russian strategy of how Russia would be integrated into the EU. The active partner in this respect would be Russia, who should voluntarily and consciously harmonise its legislation with that of the EU, not the other way round. The problem is that the process is not automatic but Russia has to have the political will to do it. It had this will in 1994 (when the PCA was signed) and although there are not many coercive instruments to implement the PCA, it is regarded, or at least can be interpreted, as a binding international agreement according to international law and both EU and Russian domestic legislation. This legal approximation approach between the EU and Russia is based on Title VI, Article 55 of the PCA. It states: “Russia shall endeavour to ensure that its legislation shall be gradually made compatible with that of the Community.”

The prioritised areas mentioned in the PCA are as follows: Company law; company accounts and taxes; auditing regulations; banking law; financial services; rules on

competition; public procurement; indirect taxation: custom laws; technical rules and standards; conformity assessment; the protection of workers at the workplace; the protection of health and life of humans, animals and plants; environment protection; consumer protection; nuclear laws and regulations; energy; transport; telecommunications; and “several other branches” of industry and agriculture. The process of legal approximation and regulatory convergence is also understood as one of the basic instruments of implementing the CES. Consequently, also the joint *CEES Concept paper* from 2003 (III, 15) and the *CES Road Map* (See *Table 2*) from 2005 list the same issue areas.³⁵

However, there may be some mechanisms to provide Russia with the possibility of affecting European legislation informally during the preparatory phase and not only blindly adapting its own legislation to that of the EU³⁶. During the earlier phases of European integration, association was considered as one of the possible ways in which a country could integrate into the EU (EEC/EC) without full membership. Following this train of thought, some mechanisms were proposed by legal specialists of how an associated country could have the possibility of consultation in preparing European legislation without becoming formally involved in Community decision-making. After that the associated country would voluntarily harmonise its own legislation. This kind of mechanism, in one form or another, could perhaps be developed between the EU and Russia.

It is also worthy of mention that between the EU and Russia the vocabulary used is “approximation” or “regulatory convergence” and not total “harmonisation”. Thus, Russia is not supposed to adopt European legislation as such, but to consider the Russian particularities also. Moreover, European legislation is only one part of the legislation of EU Member States and a lot of competency and sovereignty is still at the level of national parliaments even within the EU. Similarly, only part of Russian legislation need converge with EU legislation.

Nevertheless, what remains to be proven is Russia’s willingness to implement the legal approximation article of the PCA, which would require new mechanisms from the Russian legislative bodies to ensure the compatibility of Russian legislation with its European counterpart. Should Russia sincerely try to approximate European legislation,³⁷ a further challenge would be to create formal or informal mechanisms of communication already implied in the preparatory phase of EU legislation.

Currently, the legal approximation approach is not applied in any systemised way and there exist neither formal controlling mechanisms nor time schedules which would ensure that the relevant parts of Russian legislation would be harmonised with those of the EU. However, a starting point to this effect might be the so-called “regulatory dialogues”, which the EU has opened with certain countries important to the EU. With Russia this started in the fields of Financial Services, Intellectual Property Rights and Public Procurement in 2006. However, it was a question of only some individual meetings, where information was changed, rather than any institutionalisation of legal approximation. In any case, the idea is to continue these dialogues in 2007.³⁸

Problem solving or tinkering at the margins?

The discussion above shows that the CES is potentially a rather novel combination when compared to traditional forms of economic integration. It seems to incorporate some elements of a FTA, but excludes the customs union. At the same time it has some features of a single market, and through regulatory convergence it also includes some elements of an economic union. But, ultimately, it fails to fulfil the criteria of any existing form of economic integration.

Two rival hypotheses could be proposed on the basis of this ambiguity of EU-Russian economic relations pictured in the previous sections. First, the flexibility of the CES can be seen as its strength, creating a more dynamic process in its attempt to deepen EU-Russian integration. The *rationale* for this interpretation is that a rather technical sector-specific approach is more preferable than easy agreement on idealistic goals that would be unlikely to proceed beyond conceptualisation thus repeating the rather unsuccessful experience of CIS integration. Overly optimistic goals would only overburden the process by focussing on too

many unsolved (and unsolvable?) problems. Instead, embarking without a map upon the long road of practical and area-specific problem-solving will, by definition, show where the road ultimately leads.

One might however also claim that the lack of a clear-cut goal and a plan for its implementation in the current context of the CES is exactly its weakness, leading to half-hearted compromises and exceptions rather than to real integration. At the same time, the vague CES concept allows both sides to continue indefinitely the diplomatic game of pretending that the building of their closer relations remains a project in progress.

3. Three sectors between integration and protectionism

The above sections have reviewed the general Russian policies towards European integration. Dealing with concrete sectors of economic activity in Russia allows us to delve far deeper in terms of characterising the current situation and identifying future perspectives. In this report, three sectors are reviewed: truck transport, ports, and the forest industry. The following sections outline the main tendencies, challenges, official strategies, actor networks and decision-making practices of these economic sectors, with a territorial focus on Northwest Russia (and the neighbouring Finland and the Baltic States) in particular. (See [*Figure 1*](#))

International road transport³⁹

One of the most obvious signs of integrated societies is that the borders between them become transparent or almost invisible. From this perspective, Russia and the EU are far from being integrated. Instead, in spite of geographic proximity, natural transnational communication between the people of the EU and Russia is still regulated by a rather complicated and expensive visa regime. This itself naturally creates a lot of practical cooperation problems in trade and economic cooperation as well as in all other fields of interaction. Moreover, it also contributes to the isolation and alienation of Russia from Europe.

As to the issue of economic integration in particular the first physical precondition is that goods are moving between the societies. From this perspective looking at the international truck transport sector becomes most interesting. It is shown below – the focus being on Russia’s policies in particular – that there are several factors here that are problematic. First, Russian strategy in this field is based on the idea of a close integration of the Russian and European road transport networks and on Russia eventually becoming a central road transport link between Europe and Asia. The reality is however that Russia’s road network is currently simply not up to this task while any attempt to address this situation quickly – given the huge territorial expanse of the country – is doomed to fail. Another challenge here is that Russia’s general willingness to be integrated into Europe in this field is accompanied with a perceived need to protect its own domestic road transport sector from foreign competition by using non-market administrative measures.

Russia’s truck transport strategy

Russia’s strategy and policies on (international) road transport is expressed in the federal, federal district level and regional programmes and corresponding legislation. The basic strategy document, which determines the main directions for a long-term period, is the *Transport strategy of the Russian Federation for the period up to 2020*⁴⁰, approved after several years of debate by the government in 2004. In relation to road transport, it proclaims a “rational integration” of Russia into the surrounding environment, thus emphasising the need to protect the Russian domestic transport sector against foreign competition. Other, shorter-term programmes and strategies, such as *Modernization of Russia’s transport system (2002-2010)* or *Strategy of development of Russian Federation’s transport for the period up to 2010*⁴¹ put forward the same basic policy line.

Russia as a transport link between Europe and Asia?

In international conferences those officials and politicians who are responsible for Russia's transport policy, picture ambitious plans with Russia as a transport link between Europe and Asia. In the above-mentioned long-term transport strategy this is expressed as, "the realization of the geostrategic mission of Russia as the natural bridge between Europe and Asia".

For this to become possible Russia has to develop its road network system to match European standards. Notwithstanding this aspiration however one of the enduring themes in Russian debates on this issue has been that it is simply not rational for a country like Russia, with its huge expanse and many sparsely populated areas, to aspire to having its whole road network raised to the European standard level. As such then modernization would focus on the main highways and especially on those connected to so-called international transport corridors.

According to estimations made at the Ministry of Transport of RF, only about one fourth of Russian roads connected to Western Europe fulfil "international requirements". Moreover, the proportion of highways that correspond to Russian normative requirements decreased toward the end of 2005. Thus only 37% of the total corresponds to Russia's own requirements. At the same time the share of the roads functioning on or above overload increased in comparison with 2004.

At the strategic level existing plans for new road building projects look quite extensive. Both in the above-mentioned main long-term transport strategy and in a more detailed way in the federal programme on the *Modernization of Russia's transport system* the prioritised highways subject to extensive modernization or construction are mentioned and some budget lines are prepared. The state-owned company *Rostransmodernizatsija* is tasked with ensuring implementation of the projects.

In practice however actual funding has been much more modest than the proposed budgets lines. Therefore in Russian debates on transport issue it has often been proposed that the federation should take responsibility for modernising at least one of the main roads that connect Russia to the European Union. The idea here is that this road would serve as a "model" and set standards for other main roads.

From the perspective of international road transport corridors the strategy of concentrating on major highways might well be enough. In practice the international road transport corridors are very centralized in terms of territory; they target mainly only three federal districts out of seven. Ninety per cent of all transport is cargo transport, imported into Russia, and about 80% of the cargo exported falls to the Northwest, Central and Siberian federal districts.

Northwest Russia as an international transport junction

Northwest Russia plays an important role in Russia's road transport strategy in general, especially as its road network is directly connected to European networks. (See [Figure 5](#)) Apparently for this reason, Russian transport officials have declared that Northwest Russia is a prioritised pilot area, which should provide a model for the development of other federal districts.⁴²

In *Northwest Russia's federal district's social-economic strategy up to 2015* (2002)⁴³ all means of goods transport (both domestic and international) are anticipated to increase year on year. (See [Table 4](#)) While the biggest growth in transport of goods will take place in the maritime transport due to the increase in port capacity, which in turn will be reflected in increase also in railway transportation connected to the ports, the individually most important mean of transport will remain to be the road transport by trucks if calculated in tonnes. According to the strategy's calculations, 60% of all Northwest Russia's goods transport takes place by roads in 2020, amounting to 645 Million tonnes annually.

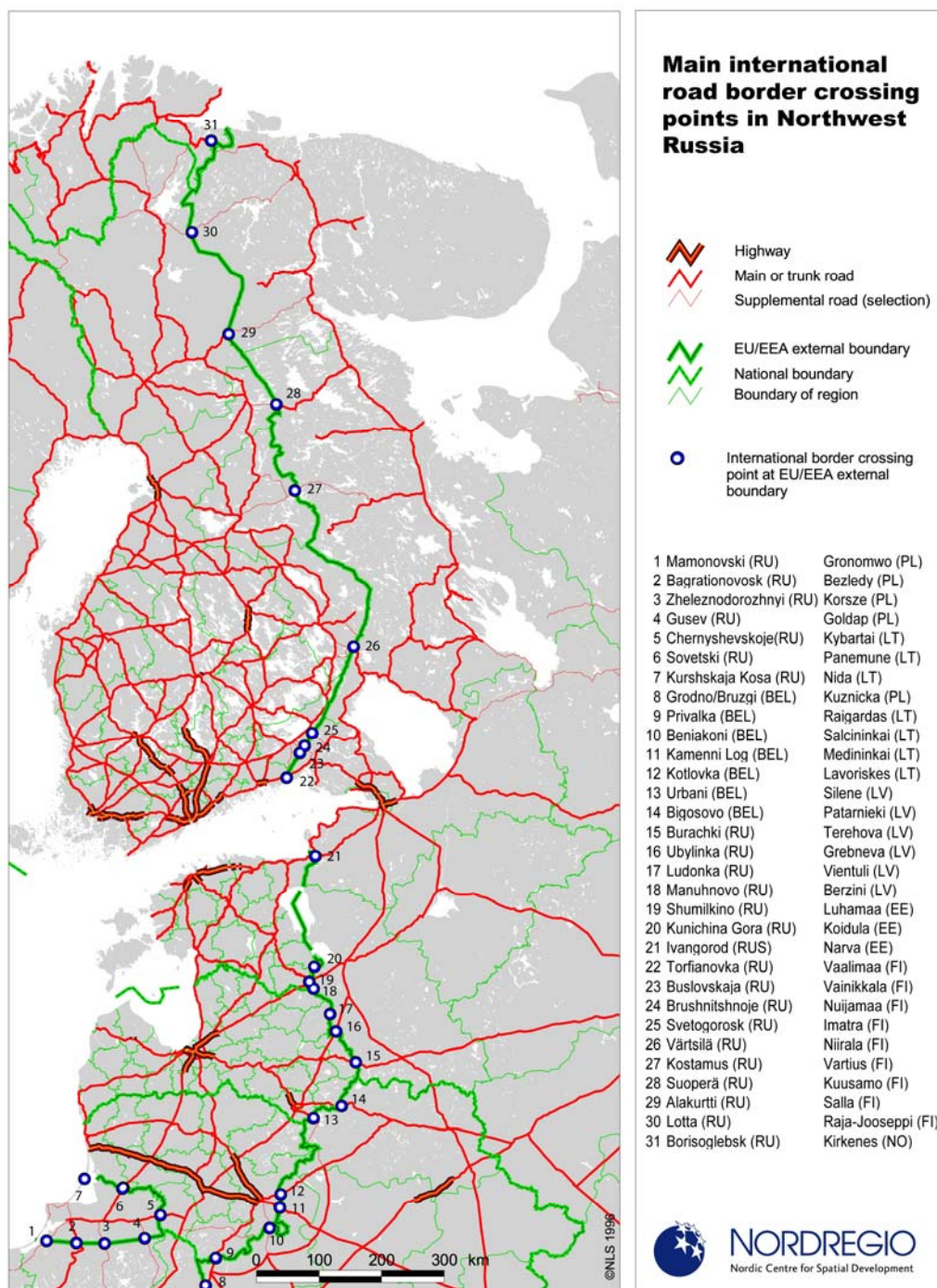


Figure 5: Main international road border crossing points in Northwest Russia

Table 4 Forecast on the growth of Northwest Russia's goods transport⁴⁴ (% / year)				
Means of transport	2010		2020	
	Domestic	International	Domestic	International
Railway transport	2,5	3,0	2,2	2,5
Road transport	3,5	4,0	2,5	2,8
Inland water transport	2,0	-	2,0	-
Maritime transport	6,0	10,0	5,0	6,0
Air transport	3,0	5,0	4,0	5,0

The road network in public use in Northwest Russia altogether runs to about 75 000 km. Public roads in Russia are divided between those administrated by the federation and those by the regions. In Northwest Russia, there are about 5 000 km (7%) of federal roads and 70 000 km (93%) of regional roads. The backbone of the road network consists of the 16 federal roads in addition to some main regional roads.⁴⁵

In Northwest Russia in particular the burden of the federal main roads is growing; the largest growth has taken place in the Kaliningrad region towards Poland and Germany, though between Northwest Russia and Finland/Scandinavia truck traffic is also increasing by many percentage points per year. Consequently, the traffic infrastructure in Northwest Russia has been much improved in recent years. The planning and construction of ring-roads around St. Petersburg, Vyborg and other population centres is part of this development work.

As the state's resources are obviously not large enough to quickly modernise the whole federal road network, other solutions have been proposed. The so far somewhat unrealistic idea that has emerged is that this huge road construction project, which would make the "Russia as a bridge between Europe and Asia" mission possible, would be realised through the attraction of extra-budgetary funds based on state-private partnership. Investors, both domestic and foreign, could, for instance, get special rights to run services, such as gas stations, restaurants etc., connected to the highways. Another proposed financial solution is to introduce highway tolls. The end result will probably be some kind of combination of each of these approaches.

Protecting the interests of Russian truck enterprises

Even if integration of the European-Russian road transport systems is welcomed by Russia, and a specific EU-Russian "ransport dialogue" institution exists to this effect⁴⁶ connected to the CES, in practice integration also brings with it new problems, which lead to protectionist policies. As one of its main policies in this field Russia has reiterated that it is the state's responsibility to defend the interests of its own road transport sector against foreign competition while guaranteeing the domestic enterprises' ability to function in changing conditions. In the above-mentioned Russian transport strategy, this is expressed as an effort to increase "the proportion of Russian transport companies involved in the maintenance of exported and imported goods traffic, and also in the transportation of cargo to and from third countries."

The Russian transport sector is, in general, characterised by the monopoly position and state protection of railway transport, while the truck transport sector has also had to compete with the railways in these unfavourable conditions in respect of international transport. Today truck transport deals, approximately, with 25% of the *foreign trade* turnover

of Russia on the value of commodities. In the *Russian-EU trade* the road transport's share is currently smaller, but at least the EU in its *Country Strategy Paper 2007-2013, Russian Federation* anticipates that already by 2010 the "total share of goods transported by road is expected to increase substantially over the next few years from the present c. 10% to a proportion [...] of almost 50%."⁴⁷

While the Russian state has not been willing to change the domestic competition structures currently favouring railway transportation at the cost of road transport, it has been more active in trying to limit foreign competition in the field of international road transport. Russia's government has tried to affect, through legislative and other administrative means, the competitiveness of Russian road transport enterprises as compared to foreign transport companies working in the field.

The Russian mainstream argument in respect of these transport debates is that protectionism is needed in order to defend the re-emerging Russian transport sector against much stronger foreign transport companies in the field of international transport. In the above-mentioned main governmental long-term transport strategy it is noted, in respect of the road transport sector, that the strategy provides for "the basic directions of state support of domestic transport organizations working in international markets, including a guarantee of protection for the most under-developed segments of the domestic transport market in the period preceding Russian entrance to the WTO".

These protective measures are usually connected to licensing arrangements, technical regulations or the taxation status of the transport companies. It seems then that Russian officials have, in this way, partially managed to move cargo from foreign transport companies to Russian ones, more so if we calculate trucks (the Finnish practice, for instance) and less so if we calculate tonnes (the Russian practice). However, while the share of Russian companies has grown, due to the overall increase of international transport in Russia foreign companies have also increased their share in absolute terms.

One of the problems for Russian trucks competing in international transport has been the rather strict environmental requirements of the EU. This has forced Russia to make an effort to adapt to the European emission standards (Euro 0 – Euro VI). While currently Euro II is the internal norm in Russia, the idea here is to move step by step to tighten the requirements for Russian domestic production as well as imported cars.⁴⁸

Russian trucks participating in international transport are clearly of a higher quality than the average Russian truck in terms of environmental standards etc. The Russian solution to this truck quality problem however reflects the contradictory character of Russia's integration policies, which forces the authorities and decision-makers into unsustainable compromises. In order to increase the quality of Russian trucks to match international standards, the federal government has lowered the import customs duty on foreign vehicles, so that the Russian companies could afford to buy them and thus compete with foreign companies. This growing import business necessarily however damages the Russian truck production industry, especially the famous production companies *Kamaz* and *Zil*. To solve this problem, in turn, much higher customs are now levied for imported used vehicles older than seven years of age thus restricting their import.

One solution to the quality problem, proposed in Russian debates by the Northwest Russian federal district representatives in particular is that the lack of truck capacity fulfilling the EU norms could be temporarily solved by building terminals, in close proximity to border crossings, where trucks without international transport licenses could be off-loaded onto more suitable transportation which could then continue with the cross-border traffic. This system has been tested at the border between Ivangorod and Narva, in Estonia, but has yet to be adopted as a permanent practice.

Actors and decision-making in the Russian road transport sector

The federation is the main decision-maker in respect of Russia's (international) road transport policy, especially as the main highways are federally owned and administrated. However, in recent years, lower level administrative entities have increased their influence in this area.

The ownership structure of the truck enterprise sector as a whole is very fragmented though there are now increasing tendencies towards market coagulation into a smaller number of dominant companies. The international truck transport sector is also rather well organized and through its interest organization can influence policies at different levels.

The federal authorities make the main decisions

Decisions in respect of transport routes, the modernization and construction of highways, traffic junctions and logistical centres are all made by the federal authorities. The role of the government is to confirm the general strategic goals and to function on behalf of Russia in relation to international financial organizations. While several ministries are actively involved in developing Russia's transport policy, the Ministry of Transport is the main actor responsible for the preparation of federal legislation and the various strategies and programmes.

Within the ministry there is a separate department for truck transport. Furthermore the Russian traffic control authority, the RTI, is subordinated to the ministry, and is responsible for vehicle licensing for different types of vehicles, among them both Russian and foreign trucks. The State *Duma* and the Council of the Federation, that is, both chambers of the Parliament, also play rather important roles at the federal level, since the legislation that concerns the sector – such as customs codes, laws on federal taxation and concession etc., – has either been rewritten recently or is in process of being rewritten.

At the very practical level another important actor in terms of international road transport is that of the Federal Customs Service, which performs the functions of control and supervision in the field of customs and other related fields. The Service, now infamous in respect of several high-level corruption scandals in recent years, is under the jurisdiction the Ministry of Economic Development and Trade of the RF. Its regional office in Northwest Russia, for instance, can affect international truck transport by maintaining the so-called white and black lists. Those blameless companies, who are included in the white list, face simplified custom duties procedures.

The seven “super regions”, that is, the federal districts, also have some impact on the international transport sector. This is particularly visible in Northwest Russia, because, as mentioned above, its transport routes are connected to Finland, the Baltic countries and to Poland. The federal districts do not have budget authority, but they can play a role, for instance, by ensuring that regional legislation is in line with the federal code (which was the main motivation for the establishment of these administrative bodies in the first place). Furthermore, the Northwest district has made an effort to draw a more detailed regional picture of the district's role as an integrative junction between the eleven Northwest regions as well as between Russia and the European neighbouring countries.

While the main highways are administratively in federal possession, most of the roads and related infrastructure belong to regions. The regions have some ability to influence the road transport sector using these roads. These include, modernizing roads or building ring roads which bypass city centres, taxation and the regional legislation. Some regions, such as the capital, Moscow, have their own truck transport strategies, aiming to limit the negative consequences of truck transport (traffic jams, environmental problems, damages to the road infrastructure etc.) and to promote the sector in order to generate budget income from taxation and other fees.

The regions have different practices as to how much they collect in terms of taxes from the transport sector. For instance, the Leningrad region is considered to be rather transport friendly, while St. Petersburg and Moscow are known for their propensity to tax heavily the

transport sector. Taxation levels thus have a direct effect on transport companies' choices of their place of registration.

Since the transport sector is traditionally regarded in Russia as a "strategic field", particularly in terms of maintaining a functioning economy, smaller local actors such as the municipalities have not previously played a decision-making role in this field. This situation however began to change in the 1990s and now municipalities have some say in their own local traffic solutions and the respective infrastructure. A new feature here is that some municipalities have put in place an institutionalised arrangement to exchange opinions with the Ministry of Transport on traffic and transport solutions. Those municipalities located in proximity to federal borders are also allowed to enter into limited transnational cross-border cooperation with neighbouring countries in respect of transport issues.

Thus, on paper, the road transport administration in Russia seems to function rather smoothly. In practice however the situation is rather less favourable. One of the problems here in respect of international road transport is, for instance, the very complicated Russian border administration system and the respective regulations, routines and payments, which contribute to making the international border crossing points a substantial bottle-neck of EU-Russian trade. (See below the case of Finnish-Russian border).

Towards a more transparent but centralized ownership structure⁴⁹

As to the ownership structure, the Russian road transport sector today remains highly fragmented. During the 1990s the sector was dominated by two different types of companies. Firstly by the small and medium-sized companies born out of the privatisation process that saw the dismantling of the large Soviet transport companies. These firms were primarily active in the domestic market and, if connected to international transport routes, they were basically import-oriented. Secondly, a number of export-oriented and rather large companies emerged, which were, and some of them still are, almost entirely state-owned. After losing the market monopoly, the big former state-owned companies, which previously belonged to the then Soviet Ministry of Foreign Trade (*Sojuzvmeshtrans* and *Sojuztransit*), did not, however, manage to compete with the first small private companies, which had soon grown into medium and then large-sized transport companies.

The result of the competitive nature of the domestic market is that the transport sector is today largely dominated by private companies. The current orientation is to continue the privatisation of the still state-owned companies. This is not taking place very quickly however; only a very small percentage of those state-owned companies offered for privatisation are actually privatised annually, which shows that the sector is not considered very profitable.

The road transport sector does not have a similar kind of elite of rather small number of actors as in energy, metallurgy and other oligarchic fields. Instead, there are innumerable transport companies, in St. Petersburg alone about eight thousand exist. It also seems probable that the sector as a whole will never achieve a major position in the Russian economic structure and therefore the companies in this sector will also basically lack political significance except perhaps in the particular field of road transport questions.

About 3000 companies in Russia have a licence and vehicles to carry out international transport, which is less than ten per cent of all transport companies. It has been estimated that in the whole of Russia only 18 000 trucks would be entitled to undertake international transport, which is regarded as a rather small number (compared to much smaller Latvia, for instance, where there are approximately 12 000 trucks participating in international transport).

Freight forwarding companies are important especially in international transport. This market in Russia consists of specialized and general forwarding companies. In Northwest Russia, there are about 80 freight forwarding companies. Among these companies there are those who concentrate only on freight forwarding duties though most also have their own

truck capacity. These companies prioritize their own trucks while also offering services for others.

The acknowledged problem of the sector is corruption and continuing connections to organised crime. Small- and medium-sized companies in particular often remain completely un-transparent in respect of their organization and economic activity. In international transport, criminality often takes the form of violating customs regulations. In Northwest Russia alone, several hundreds court cases take place annually concerning customs violations, taxation violations and so forth. In a major part of the cases, corruption undertaken by the authorities themselves is part of the crime.

In Russian debates on criminal practices in the transport sector, one of the main arguments is that the freight forwarding companies and the other large transport companies would be interested in creating transparent rules and practices in the sector. They find it particularly difficult to compete with small- and medium-sized companies, who do not pay taxes and do not follow the regulations. Thus their self-interest should drive toward the quest for more transparent practices while at the same time delivering a more centralized transport sector.

Some foreign transport companies have affiliated companies or offices, which are registered in Russia in order to avoid the protectionist regulations (among them about thirty Finnish companies, some of them have been working in this way for more than a decade). In principle they then become Russian companies, but usually with licenses only for international (and not domestic) transport services. Furthermore, it is estimated that from CIS countries there are, in addition to the legal ones, innumerable illegally operating trucks operating throughout the Russian Federation.

Institutionalised interest group influence

If the transport sector cannot influence political-administrative decision-making via informal networks as is the case within the oligarchic industries, it nevertheless can influence it through its interest organizations, at least to some extent. The Russian transport sector was already organised into interest groups during the Soviet era though today the nature of these activities is considerable different. While there are several interest organizations related to road transport, the main organization in the field of international road transport in particular is the Association of International Truck Transport (ASMAP)⁵⁰, established over thirty years ago, with currently about 1500 member companies (that is, about a half of those roughly 3000 identified companies who deal with international road transport). It tries to function as the sector's interest organization in respect of all Russian authorities and international actors in the field.

ASMAP has managed to institutionalise its relations with the government and with the Ministry of Transport in particular. ASMAP has had a central interest group role in the preparation of the new legislation related to the field – such as the *Customs Code* (2004). ASMAP's special concern has been to protect the Russian companies' positions in the international transport market, and, according to its own testimony, this effort has been successful. Its chairman regularly presents their views in the so-called enlarged meeting of the ministry's *collegium*. In these meetings the ASMAP representative usually reviews and discusses the conditions for Russian and foreign transport entrepreneurs, the market situation between them, and advises the federation on the modernisation of the transport routes which connect Russia to the EU. ASMAP is also represented in those working groups and committees of the Russian transport authorities which meet with their foreign counterparts.

Within Russia, ASMAP has however been rather critical of those authorities who do not follow its recommendations. For instance, it claims that the Ministry of Industry and Energy is too slow in establishing regulations and conditions for the domestic automobile industry that would enable it to reach the Euro III and Euro IV levels, which hinders Russian enterprises in their efforts to increase their market share in terms of international road

transport. Another example here is that ASMAP has also heavily criticised Moscow for following a much harder line of taxation in respect of the transport sector than that laid down in the federal priorities.

Towards a multilateral solution?

In respect of the international arrangements, the most important organization here is the International Road Transport Union IRU, which comprises 68 countries. Through ASMAP Russia has been a member since 1975. In 1998 the IRU opened an office in Moscow. It is from here that it coordinates its action in the whole CIS area. Russia is also part of the IRU's *TIR-Carnet* customs system, allowing the custom duties for a sealed cargo to be paid at the destination instead of at the border.

One element of the TIR system is the IRU's guarantee fund for those custom fees, which are not received if the cargo disappears before the truck arrives at its destination – which happens frequently in Russia. While the Russian Federal Customs Service has tried to get compensation from this fund the IRU has accused the Russian authorities of protecting, or at least being passive towards, organized crime. At times there have been rather heated arguments between the Russian authorities on the one hand and IRU on the other, but Russia has nevertheless remained a participant in the TIR convention.

Another multilateral transport arrangement would be Russia joining the Common Transit Convention, which in the EEA sets out the requirements for the use of the Single Administrative Document (SAD), a unified customs document. In principle, this would bring Russia considerably closer to the EU in the field of international transport and customs. According to the EU's *Country Strategy Paper 2007-2013, Russian Federation*, "Russia has expressed strong interest in joining the Transit Convention, although the development of the necessary administrative and technical capacity will take some time."⁵¹

Excursion: The case of the “truck quarrel” between Finland and Russia⁵²

The issue of Russia’s international truck transport trade over the Finnish-Russian border is highly illustrative from the point of view of EU-Russian relations. Even if the Finnish-Russian border is usually presented as a model for the EU-Russian border regime, the border generates a substantial bottleneck in trade terms between the countries.

This short “case” shows that Russia’s real integration into Europe presents a considerable, and even physical-spatial, challenge for both sides. In addition to the technical and bureaucratic problems many elements of a permanent trade policy conflict are bound up in this question.

Growing importance of border crossing

Due to the common border of about 1300 km, road transport has always been important for Finland’s trade with its eastern neighbour. Currently there are nine international border crossing points between Finland and Russia, of which *Vaalimaa* and *Nuijamaa* in the southern part of the border are the most important. (See *Figure 5*) Russia’s significant economic and industrial growth in the past few years and the fact that it has recently become Finland’s largest trade partner (before Germany and Sweden) has further increased the salience of road transport between the countries.

The size and structure of exports and imports in Finland’s trade with Russia are rather different. Finland’s exports consist mainly of value-added products, while imports are dominated by energy, wood products and other raw materials. Road transport is particularly important in the context of Finnish exports to Russia as about 70% goes by road. Nevertheless, in absolute terms the volume of Finnish imports from Russia is about sixteen times larger than its exports, and while in relative terms road transport takes up only about 13% of all imports, in absolute terms road transport is three times larger in tonnage terms as compared to exports. On top of this comes the rapidly growing transit transport on roads via Finland to Russia. As a whole, truck transport between Finland and Russia is growing by almost ten per cent annually.

Calculating trucks or tonnes?

While growing trade interdependence can be identified this does not come without problems. Road transport in particular has occasionally resulted in rather sharp quarrels emerging between each country’s authorities and other actors. While both parties acknowledge that the situation is not ideal, as with most international disagreements, blame is not usually one-sided. The principal starting point for the officials of both countries is the defence of their own country’s transport enterprises.

From the Finnish perspective, the Russian authorities have with protectionist and arbitrary treatment and via the violation of international agreements, discriminated against Finnish (and other foreign) transport companies in the field of international road transport in Russia. From the Russian perspective, Russian road transport enterprises are in a weaker position and therefore the Russian state has the right to use protectionist measures in order to defend their economic activities against foreign transport companies.

One of the problems here is that Finland and Russia use different methods in their evaluation of the truck transport shares from the perspective of their country of origin. In Finland one counts trucks while in Russia one counts tonnes. The situation and in part the nature of the market development looks rather different depending on which way one calculates, since Finnish-registered trucks are usually much heavier than the Russian ones. Comparable information is however difficult to find while it seems that neither country has all the necessary information to hand.

In the conditions of a liberal market economy, it is, of course, not in principal a problem if one country's transport enterprises dominate the field. It is acceptable that Russian entrepreneurs, for instance, benefit from the probable lower price level and special knowledge of Russian road transport, while Finnish entrepreneurs benefit from better vehicles and perceived better reliability and accountability. The real problem thus arises when market conditions are distorted by protectionism and arbitrary administrative practices.

Three kinds of concrete questions, in particular, have been tabled in respect of this ongoing disagreement. First, technical questions related to the trucks; second, customs formalities and duties; and finally, transport quota permissions, that is to say, how many trucks are allowed to pass the border.

Technical incompatibility

The technical questions of truck transport between Finland and Russia have played a visible role in the Finnish media, since they have mostly been applied to Finnish trucks by the Russian border authorities. The main issue here concerns the weight and other physical limits of the trucks. The underlying problem is that EU/Finland and Russia have rather different and often incompatible requirements in the field of road transport and correspondingly for the type of trucks that are to be used.

There is however no stable Russian practice to refer to in the definition of these technical standards. A figure of 38 tonnes used to be the limit for trucks to Russia, which is the general weight limit for most of the roads in Russia. At times the weight limit has been increased to 42 tonnes. Should a truck weigh more, a special permission certificate with corresponding fees is required. In principle, trucks heavier than 44 tonnes should not have been accepted at all, but Finland has negotiated special arrangements in this respect and has managed to negotiate for itself the right, in the context of round wood transport (and earlier also in respect of other transport), trucks up to 55 tonnes. These arrangements have included detailed restrictions concerning the roads to be used.

Controlling and changing the rules has been a favourite instrument of the Russian authorities. Russian rules, or more precisely their interpretation have often however been changed without advance information such that the Finnish trucks have been unexpectedly ordered to pay penalties or additional costs, or turned back at the border. Often no reason is given for such sudden changes; and if it is, it has usually said to be the bad condition of roads and bridges, which would not sustain heavy loads, or alternatively, changed administrative practices, "orders from above" are cited.

While in the Finnish debates the main argument is that Russia is using technical requirements for discriminatory purposes, in the Russian debates the opposite is argued; it is Russia, who in fact has yielded to Finland on many questions, for instance, in allowing overweight 55 tonne trucks. The Finnish authorities have replied, in turn, that the Finnish 55 tonne 7-axle full-length trucks do not overload the roads more than the Russian 44 tonne 5-axle half-length trucks.

When the disputes have come to a head, the Finnish authorities in their turn have occasionally reacted by undertaking officious and thorough technical control of the Russian trucks at the border, or by demanding for instance international insurance documents that have not previously been required.

Bureaucratic custom duties

A second type of dispute concerns customs duties, namely that it takes so much time at the Russian side of the border. In the Finnish media, this has been reflected in repeated news about huge truck queues at the border, at times reaching 50 km in length on the Finnish side, causing not only trouble for the companies concerned but also constituting a major traffic safety risk as well.

Russian transport interest organizations have also however been very animated by the same problem; according to them, about 30% of the transport time of Russian trucks in international traffic is spent going through customs and other border formalities.

Basically then this is not an issue directed specifically to Finnish or foreign trucks but is rather a general problem relating to issues of the poor organization of the Russian border formalities in the context of road transport. The Russian authorities acknowledge these problems. Nevertheless although the problems have continued for many years the situation has failed to improve markedly.

In a 2005 report of a test commissioned by the Finnish Ministry of Transport and Communications⁵³ with 12 Finnish or Russian registered trucks, a truck coming from Finland to Russia had to deal with up to 8 different Russian border authorities, compared with just 3 on the Finnish side, and while the documentation of a single truck was handled 5 times by the border officials on the Finnish side, on the Russian side of the border this number rose to up to 52 times!

In principle, the Baltic Sea countries have agreed on a target of a maximum of two hours for crossing the border. In the test, only one of the twelve trucks achieved this goal, while the longest waiting time was more than 16 hours. Most of the waiting time was spent in a queue waiting for the Russian officials to begin their inspections. Coming from Russia to Finland, everything went much more smoothly, but not as quickly as on the Finnish side in both directions.

While the practical bureaucracy takes time, it also seems that the internal relationship between different Russian authorities at the border is unclear, and in these conditions the decisions on, for instance, the turning back of or ordering penalties for a truck may be rather arbitrary or accidental. Furthermore, it has been proved that both Russian and foreign trucks are sometimes also objects of illegal fraudulent activity on the part of the Russian authorities, who want to collect extra payments, which may take place, for instance, in connection to the weighing of transport.

State regulation of transport quotas

A third issue in this bilateral “truck quarrel” has been the number of annual quotas for transport. This administrative, regulative instrument has been particularly useful in the hands of the Finnish authorities as the quotas are usually based on the same amount of trucks for each country; counting the trucks (instead of tonnes), Russian trucks are more numerous.

The practice – reflecting the Finnish transport authorities’ concern they should not give away negotiating power which could be used in sudden crises in Finnish-Russian road transport connections – has been that the transport authorities negotiate on the quotas issue several times during the year (instead of negotiating the quotas for the whole year), and thus transport licenses are therefore granted piecemeal.

Possible solution-generating forums?

There are several levels where one could try to find solutions to the above-mentioned practical problems between the EU/Finland and Russia in terms of transport issues.

First, there are *multilateral* levels to simplify the customs bureaucracy. One could imagine that the so-called EU-Russia Transport Dialogue, especially its Working Group “Road and Rail Transport” or the PCA Sub-Committee on “Customs and Cross-Border Co-operation” could work as a forum where exactly the above types of problems between the EU Member States and Russia could be discussed and resolved. As these institutions seemingly are impotent to work effectively in these questions, however, one should try to find out how it could be improved so that the Member States’ and Russia’s joint problems could be solved. (See the concluding section)

While the EU-Russian transport dialogue level seems not to work, a more effective forum is the International Road Transport Union (IRU), working at the *transnational* level. As one of its main features, Finland and Russia, both being members, utilise the TIR-Carnet system which means that a TIR transit sealed in the departure station will not be controlled at the border but only at the destination station.

The TIR convention has however not functioned flawlessly at the Finnish-Russian border, and Russian customs authorities have opened TIR-sealed truck without proper authority on a number of occasions. Both the IRU and the Finnish interest organizations have protested at these actions and the Finnish truck transport drivers' interest group AKT has organized loading boycotts for Russian trucks as a counter measure.

However, as many of the border-crossing problems are common to both EU Member States' and Russian transport companies, such as the too complicated customs duties and extensive delays on the borders, there should be no principal obstacle why the sectoral interest organizations such as the Russian ASMAP, Finnish SKAL or the transnational IRU could not work together to solve the common problems, trying to pressure the authorities of the EU and Russia to find solutions. As of today, it seems that the national interest organizations are much more interested in their "national interests" than solving joint sectoral problems.

Potential *bilateral* solutions between Finland and Russia also exist, and actually the authorities of both countries' transport ministries meet regularly several times a year at different levels, accompanied by the respective interest organization representatives. In these negotiations, for instance, in order to overcome the bottleneck at the Finnish-Russian border, a Green line system has been introduced in 2003. This system is limited to only some Finnish (and Swedish) companies. The idea here is that the necessary information is sent electronically in advance from the Finnish customs authorities to their Russian counterparts, and after only a short recognition check at the Russian customs, a TIR truck can continue directly to its final customs station.

The port sector⁵⁴

The most important transport sector related to Russian foreign trade is the port sector. As the Soviet Union collapsed about 58% of its port capacity was left outside the Russian Federation. In consequence, in its foreign trade Russia had initially to rely largely on ports in Finland, the Baltic States and Ukraine. Soon Russia, however, adopted a policy of increasing its self-sufficiency in the port sector.

Russia's port strategy

Large-scale port construction was not a short-term goal of Russia in the mid-1990s while investment in the existing ports remained low, with the exception of some Black Sea ports, which were important for oil exports. The weak investment environment was a result of several factors: a lack of capital, the unstable political and economic situation, extensive corruption at the federal and regional administration levels, and the lack of a legislative basis.

Furthermore, the existing ports proved not to be easy to adapt to the changing needs of Russia's production and foreign trade, and therefore it was estimated that the necessary technical infrastructure changes would be considerable large and expensive. The infrastructure related to the ports, such as railways, roads, energy networks and pipelines were also in need of modernization and huge investments.

Since the end of the 1990s however Russia has managed to build up its own port capacity and will continue to do so into the future. This rapid development has surprised many observers, including Russia's neighbouring EU Member States who are concretely affected by it.

The revival of Russia's commercial fleet

As in other fields, Russia's policy on ports has been presented in the form of several federal programmes and strategies, which identify and define the main problems of the field, strategic goals and priorities, needs for the further development of legislation, the relationship between the different actors in the field, and funding questions. In 1992 President Boris Yeltsin laid out, in a presidential decree, a *Programme for the revival of the commercial fleet of Russia 1993-2001*. The programme initiated the current development and Russia managed to increase its capacity during the programme period by approximately 40 Million tonnes.

As a whole, however, the programme is regarded as having been badly prepared and implemented, and it is generally acknowledged that the dynamic development of the port sector actually only really began in earnest after 1999 with the assumption of President Vladimir Putin to power.

Within a few years a renewed strategy for ports (as well as for the whole transport sector) was prepared. In 2001 the government adopted the programme *Modernization of the transport system 2002-2010*, which was partly rewritten in 2005. This is the main middle-term programme outlining the mechanism concerning the goals, priorities, responsibilities, funding and other principal issues concerning ports (as well as railway and roads). Another short-term programme is *Strategy of development of Russian Federation's transport for the period up to 2010*.⁵⁵ The more abstract long-term strategy, prepared simultaneously, is *the Transport strategy of the Russian Federation for the period up to 2020*.⁵⁶ In addition at the district and regional levels in Northwest Russia a number of programmes and strategies have been put in place aimed at the development of the port sector, and in particular at creating the necessary port infrastructure and its related transport systems.

All of these documents have been published in different versions and there has been a considerable public debate around them. Thus, the Russian port sector (and transport sector) has by no means been developed secretly, and basically the current situation has been predictable.

The existence of the new dynamic situation from the late 1990s cannot be explained only by the change of President, but rather via several parallel reasons. Firstly, Russian exports, relying on energy and raw materials, tripled during the decade. On this basis, Putin announced that the port sector is a “strategic sector”, essential for the country’s (economic) security.

Secondly, Russia had begun to look at its port sector from a more political and even a military security point of view, in response to its worsening relations with the Baltic States, whose ports it was dependent upon. The Baltic States’ membership of NATO added to this security thinking. In these circumstances Russia, having as its goal the rebuilding of its great power status, decided not to allow its major foreign trade routes to be controlled by parties, which in some – even if hypothetical – situations could be its political and military opponents.

Thirdly, by the turn of the century, as opposed to the situation pertaining in mid-1990s, capital could be found in Russia to pay for major port investments. Port privatisation was advanced and the private-owned oligarchic companies in particular, dealing with oil and other raw material exports, could now afford to pay for large infrastructure projects.

Why did the Russian companies decide to invest in ports? Outside Russia it has been argued that the Russian port build-up is only based on political calculations (of the Russian state) and that it would have been economically more rational to rely on foreign ports (that is, those of Finland and the Baltic States). Indeed, some western commentators went so far as to state that by building own ports Russia’s policies “echo Soviet autarky thinking”.⁵⁷ This argument has not however been generally accepted in Russia. According to the Russian mainstream argument, by using its own ports in Northwest Russia instead of those of Finland or the Baltic States, Russian companies save 15-50 USD/tonne and 120 - 300 USD/container. This amounts to around one Billion USD annually. The Russian state also wins in terms of taxes and other income-related issue in respect of ports on its own territory.⁵⁸

Finally, it is clear that those regions located where the ports were to be built saw these projects as greatly facilitating their respective region’s socio-economic situation, and they actively lobbied the federal decision-makers to become more active in the development of the port sector.

Building up Northwest Russia’s ports ⁵⁹

Northwest Russian foreign trade volumes constitute a remarkable share of Russia’s total foreign trade, and about 80% of all cargo through the ports network goes through the Northwest Russian ports. In recent years, the cargo volume sent through the Northwest Russian ports has also increased in absolute terms and is currently much larger than that during the Soviet era. The Northwest Russian ports moreover now compete with Finland’s and the Baltic States’ ports.

The capacity of the Russian port sector in Northwest Russia has been increased by enlarging and modernizing the existing ports as well as through the building of new ones. (For the location of the major ports in the area, see *Figure 6*) The district’s biggest and most versatile harbour entity is St. Petersburg port, which has in recent years been enlarged perceptibly, amounting for about one tenth of Russia’s total foreign trade freight traffic. In the Leningrad region (which surrounds St. Petersburg), several port construction projects have either been finished or remain in progress. The port of Vyborg has been modernised and the port of Primorsk, opened in late 2001, was connected to the Baltic Pipeline System. The new oil terminals at the port of Vysotsk, were connected by railway to Primorsk, are part of the same system. The port of Ust-Luga in the Leningrad region, currently only partly finished, is planned to serve versatile cargo while the port of Kaliningrad is to be developed to be fully compatible with other European ports. An oil terminal project has already for several years been planned and at least partially constructed at Bukhta Battereynaya, also located in the Leningrad region. A small existing port in Lomonosovo, in the Leningrad

region near St. Petersburg, is supposed to be enlarged to compete with St. Petersburg, Ust-Luga and foreign ports in versatile cargo transport.

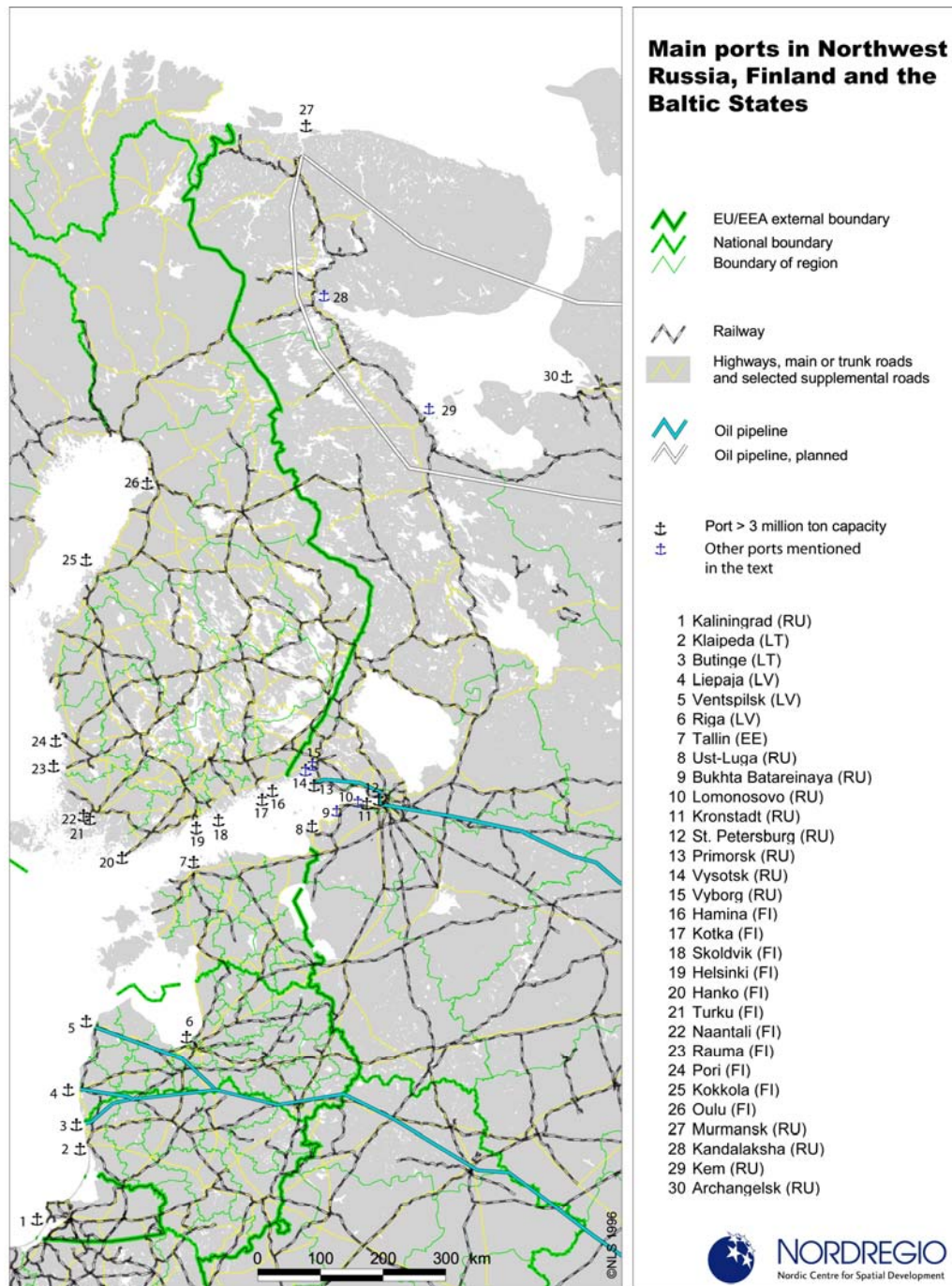


Figure 6: Main ports in Northwest Russia, Finland and the Baltic States

In future however an important role will be played also by the so-called Northern sea route, if the plans to build an oil terminal in the port of Murmansk (or a new port in the Murmansk region with oil terminal) and the respective pipeline from Siberia are realized with a view to creating a new export route to the USA. The port of Arkhangelsk is also to be

modernized and redesigned for the purposes of oil and metallurgy export. At present the rather limited amount of oil exported from these two ports is carried there by using railways or sea or river routes. Added to the above-mentioned ports, there are a number of minor ports in the Northwest Russian district, including Kandalaksha (Murmansk region), Kem (Karelia), Narjan-Mar and Amderma (autonomic district of Nenets). In addition, news about different companies' plans to build new ports and terminals in the Murmansk region in particular can be read frequently from the Russian news sources.

Increasing the competitiveness of Russian ports

Russian officials usually regard the rebuilding of the port sector as a success story as Russian ports' cargo volume has about quadrupled between 1993 and 2006. Russian evaluations of the future of the port sector are optimistic both in the short and the longer term. This is so for several reasons. First, the federal state is committed to the development of the sector because of its definition as an essential field of national security. Second, the perspective of future economic growth is good. Third, expectations concerning exports, especially of oil and raw materials, are good. Fourth, import volumes are growing in both relative terms compared to export and in absolute volumes. Finally Russia's share of the transit cargo market is growing across all type of freight sectors.

In recent years Russian Federation legislation has been developed in the spirit of supporting Russian ports in the context of international competition. This policy relates to efforts to make Russian ports more attractive for both domestic and international actors such as the lowering of customs duties and other formalities.

While the volume of cargo through ports has been steadily increasing every year by tens of percentage points, port capacity remains insufficient to satisfy the level of demand, which is growing at an even faster rate. At present Russian ports can handle about 75% of the country's total foreign trade through sea routes. This has already been estimated as constituting a minimum level of self-sufficiency from the point of view of the country's strategic security. According to the strategies mentioned above, the goal is to reach 90% self-sufficiency by 2010.

In addition to the lack of available port capacity in general, Russia's port infrastructure does not match the structure of the foreign trade. Indeed, while it matches quite well the energy and raw material based *export* structure of Russian foreign trade, it at the same time reveals that the *importing* part of Russia's business elites consists of a rather diverse non-oligarchic actors, who have either no interest in, or are too fragmented and small to affect the development of the port sector.

Nevertheless, it is estimated that in the near future Russia will be able to increase its share of value-added export as compared to its current energy and raw material dominated export profile. This together with the rising level of imports means that Russia's foreign trade will increasingly come to consist of goods transported in containers. The estimates here are of several hundred per cent increases within five next years. Russia's current container capacity simply cannot keep pace with this likely growth.

Currently considering all of the Northwest Russian ports only St. Petersburg can handle containers and even its capacity is rather limited. As such, while, in terms of volumes, the majority of Russian exports flow through Russian ports – which are specifically set up to deal with oil and raw material exports – two thirds of Russia's imports, largely consisting of value-added products, are transported via containers through Finnish or Baltic ports. Therefore Russia is loosing clients to Finland and the Baltic States particularly in the import transportation sector.

Seeing this as not being beneficial in the long run Russia's strategy is to change the market situation in container transport to its advantage. To this effort the new port of Ust-Luga in the Leningrad region will by 2007 have (in accordance with the project plans) an infrastructure capable of handling a high volume of containers.

Nevertheless, it has been estimated that it will take until around 2015 before Russia has sufficiently increased its port capacity in terms of the necessary infrastructure to a point where it would be able to successfully address these issues. This gives the Finnish and the Baltic States' ports at least an eight year window of opportunity to adapt to the envisaged market changes.

They could also try to compete with efficiency and flexibility, for instance, offering quick service, a variety of technical equipment, safe depots, links to other versatile transport infrastructures (railway and road networks) and so forth. Indeed, comparing the Baltic countries with Belgium and the Netherlands, it has been argued that the latter's positively disproportionate position in Europe's port sector "has been achieved through foreseeing local actions to organize cargo-handling so efficiently that it has not proved viable for the big neighbouring countries to hold back, or make any serious attempts to redirect, the flow of cargo."⁶⁰

With regard to Russia, however, given her great power ambitions and therefore the overly emphasised connection between the country's security and foreign trade routes, makes this task much more difficult for the Baltic countries and Finland than it has been for Belgium and the Netherlands.

Transit transport is no less important than Russian exports and imports. Russia's port strategy, like the road transport strategy, is characterised by the general idea that Russia will become a major transit hub between Europe and Asia. In Northwest Russia this presupposes that a very large development process takes place in respect of Russia's ports in the Baltic Sea, Barents Sea and White Sea up to 2015, aiming at moving the transit business from Finnish and Baltic States' ports to Russian ones. According to the estimates emerging from within the Russian debates, this should contribute at least 15 Billion USD annually to the Russian federal budget.

Russia has in the port sector also used administrative measures to increase the market share of Russian ports. One example here is the decision, motivated by an initiative of the Russian government, to cut off oil transit through Latvia to the port of Ventspils in January 2003. Latvia regarded this as a violation of the bilateral agreement from 1993 between the countries over the joint use of the oil pipeline. In any case the Russian port of Primorsk increased its market share through this action.

The environmental impact of Russian ports?

The debate over the environmental impact of the Russian Baltic Sea ports has fuelled both domestic and international concern. This question has been discussed in meetings between the federation and the regions and also in meetings between President Putin and the private sector actors. The general spirit of these discussions is to emphasise the importance of environmental aspects, while at the same time assuring all concerned that everything is in order.

In principle, Russia has the necessary legislative framework in place to deal with such issues, a framework which stipulates that environmental impact assessments are obligatory in these types of projects. The main official body responsible for this would be the Ministry for Natural Resources, into which the previous State Environmental Committee was incorporated in 2000, thus however diminishing the independent status of environmental policy actors in Russia.

In practice environmental impact assessment has had a rather subordinate role in decision-making, planning and the construction of ports, even if it is *formally* undertaken. Regional environmental officials have occasionally been quite active in monitoring the possible violations of the norms and laws but in major port projects their real impact has been limited. The national environmental impact assessment is generally done *after* the actual decision to build a port has been taken and thus its impact has proved to be minor.⁶¹

The environmental impact assessment processes do not have a transnational character in terms of properly sharing information with the neighbouring countries. The Soviet Union

did sign the Espoo Convention on Environmental Impact Assessment in a Transboundary Context (EIA) in 1991, and the Russian Federation later confirmed its signature in the form of a presidential decree in 1992 though this seems to have had little effect. The Espoo Convention sets out the obligations of the parties to assess the environmental impact of certain activities at an early stage of planning. It also lays down the general obligation of states to notify and consult each other on all major projects under consideration that are likely to have a significant adverse environmental impact across borders.

Russia has not however ratified the convention. The Ministry for Natural Resources has, at times, in its documents included the convention with those that should be followed in industrial and transport projects though *in practice* Russian officials do not follow it. Neither did Russia sign the 2003 Kiev (SEA) Protocol, which is seen as constituting an earlier phase of the EIA and requires its parties to evaluate the environmental consequences of their official draft plans and programmes as well as providing for extensive public participation in government decision-making in numerous development sectors.

In both cases Russian practice marks a visible exception to the European norm in terms of transnational cooperation in environmental protection and sustainable development.

Actors and decision-making in the Russian port sector

The network of actors in the Russian port sector has in principle stabilized in recent years while the roles played by various actors are now becoming clearer. The main lines of development in the sector have been drawn by official bodies and one can now see a certain master plan emerging in terms of how to develop the management of Russian ports and their commercial maritime activities. At the same time the privatisation of the sector is basically finalised. Nevertheless, at the practical level the political process entails numerous bureaucratic and interest group struggles, even where the main policy lines are already agreed upon.

The state defines the overall goals

The federation is the main architect of Russia's port sector policy. The state has, partly against its will, remained a rather important minority shareholder with a 10-20% stake in the ports and companies related to their maintenance and development. The federal state's main role is however to define the overall sectoral goals and functions as an arbitrator trying to adjust the state interest with the interests of other parties.

As many laws related to the port sector – such as *Customs Code* – have recently been revised or are in the process of being revised, the Russian Parliament (the State *Duma* and the Council of Federation) can be said to have actively participated in the development of the port sector proposing a considerable amount of amendments to the draft laws (prepared by the government bureaucracies). Nevertheless the executive authorities have succeeded in retaining control of policy development in the sector.

The instruments the federal state uses in controlling and directing the port sector are legislation, taxation, various strategies and programmes mentioned above, its ability to define the rules of the game in various ways, and through its control of the limited available funding from the budget.

Concrete decisions to begin a port construction project are made at the federal level, even if the concrete initiative originally often comes from the private sector, namely from the big foreign trade related companies who need more port capacity. The initiator among the federal authorities is usually either the Ministry of Transport – a special Agency of Maritime and River Transport is subordinated to the ministry – or the Ministry of Economic Development and Trade. The *rationale* for any port project is usually considered by experts of several other ministries and agencies.

The final decision will however be made by the government (and not by any ministries alone). In cases where the outcome is positive, the government budgets for its investment

share, which the federation uses for that part of the infrastructure for which it is, in accordance with the legislation, responsible. It is usually a question of relatively small amounts of financing in this respect. Federal funding is used for that part of the infrastructure development that belongs to the federation, region or municipality, and of which privatisation is forbidden by law. Concretely, this may concern the building of canals, the dredging of the seabed or establishing the port's navigation system, for instance.

The role of regions in the development of Russia's port strategy is basically limited to the implementation of federal decisions. The relationship is not really problematic however, since the regions are usually more than eager to have a new port because of its positive socio-economic impact.⁶² Regions are also usually active lobbyists for any individual port project likely to be built in their respective region. In many cases it is a question of a zero-sum competitive game between the regions, all of whom lobby federal decision-makers and big companies to prioritise their respective region. The Leningrad region competes with St. Petersburg, the Murmansk region with Arkhangelsk, and in principle the Northern Sea Route with the Baltic Sea Route also compete. For instance, St. Petersburg has been rather successful in lobbying for the rapid development of its port, which has consequently been reflected in the development delay of the port of Arkhangelsk.

Local territorial and administrative entities, such as districts and municipalities, are also interested in port projects from the same obvious reasons as the regions, but in practice they have no real influence on the decision-making process. In principle they could have some power, since land-use licenses are their responsibility while existing environmental legislation offers some control mechanisms concerning projects under planning or construction as well as port activities in general. It is however rather difficult to find practical examples proving that local actors have made a difference even in such situations.

Once the ports are functioning, the role of the authorities continues to be crucial. In the media, especially the negative factors are usually notified. Corruption, which characterizes the port sector in general, is one of the most important obstacles to market force determination of the functioning of the Russian ports sector. The customs authorities, railway services related to sea cargo and the port authorities themselves are, according to many observers, some of the most corrupted organizations in Russia. In respect of the functioning of ports, corruption is usually related to the services provided: the potential to avoid customs and formalities; accelerated treatment for certain cargoes; quicker or cheaper access to transport infrastructure. This means that those companies who adapt to corruption get quicker, better and cheaper service than those who follow legal logistics rules.

Oil companies dominate the ports

The port sector is largely owned by the private companies who use its services, especially the export oriented companies (oil, minerals, metallurgy, forestry etc.). The role of the oil companies is particularly crucial here. The *Energy strategy of Russia for the period up to 2020*,⁶³ accepted by the government in 2002, forecasts that Russia's oil production will increase to 445 Million tonnes per year by 2020, of which 290 Million tonnes will be exported. This is about 100 Million tonnes more than today.⁶⁴ The current pipeline and port capacity is barely enough for today's production and export, which means that large new investments are needed in respect of oil transport infrastructure, including the ports. Other raw material based industrial sectors, such as gas, metallurgy, coal, forestry, are also interested in the functioning and development of the port sector.

The strategy of the big companies in these fields is to build up their own infrastructure in the ports in order to, first, secure their transportation needs, and, second, to minimize export costs. This can mean building a whole port infrastructure, or in more modest form to secure own storage space or loading equipment. While serving their owners, these services can be used for other clients, too. Thus the port sector development in Russia is very closely connected to the needs of the export sector companies.

The support of the private and state-owned companies for a port project is important right from the initial stage. Indeed, most often a concrete project is initiated by the interested companies (rather than authorities) based on their strategic interests and concrete needs. Thus, the oil company *Lukoil* is, for instance, behind the Vysotsk port project, because it calculated that it will profit by 25 Million USD annually in transport costs if a port with an oil terminal was to be constructed there. The development of the port of Arkhangelsk, in turn, would not be supported by the federal government if the private company *Norilsk Nickel* and the state-owned company *Rosneft* would not have supported the project based on their profit calculations.

However, the Murmansk port oil terminal project, connected to the planned huge pipeline project, now frozen, showed that there have been, and probably will in the future, in spite of the strengthening of the state control over the energy companies, be major disagreements between private companies and the state. The principal issue, still unsolved, was whether the main pipeline to the Murmansk port would have been owned and administrated by the state-owned *Transneft*, who has the monopoly of the pipeline system, or whether this field of economic activity should have been opened to private ownership.

The most important open questions between the large companies and the state are resolved behind closed doors between the owners or CEOs of the companies and the federal government and presidential administration. Many of the issues are however of a technical character and in those issues the state interests are represented by the regions or federal district involved. The coordinating councils, established by private and state/regional actors, play important roles in this type of negotiations.

As to the issue of technical and land-use planning, the licensed planning and consultation institutions have a considerable influence over the final result. After the government decision on a port project has been made, the Ministry of Transport delegates the planning to a state-owned or private but state-controlled planning and consulting institute. Often this process is non-transparent, which facilitates corruption. Most of the institutes who participate in the development of the port sector are located in Moscow, though also some are situated in St. Petersburg.

Foreign companies have not participated to any great extent in the development of Russian ports, beside those Russian companies registered abroad for various reasons and who have for some years invested their profits back into Russia. Several reasons may explain this fact. Firstly, the privatization process of Russian ports has been one of the most non-transparent and corrupt privatization fields in Russia, and foreign companies have in principle had no access to this process. Secondly, as Russia's leadership considers the control of the ports to be an important element of the country's economic and strategic security, no large-scale foreign ownership, management and control is welcome.

Some of the big Russian export companies are in reality however really transnational corporations rather than purely Russian ones, such as the TNK-BP oil company which owns port infrastructure in Russia. Other kinds of joint foreign-Russian unions and companies have, in addition to the flow of foreign loans and foreign portfolio investments, to some extent also been able to finance the construction projects.

The role of the international financial organizations in lending money for Russian infrastructure and transport projects, including ports, used to be rather important even in the mid-1990s, and the regions still, on occasion, consider them as important sources of the financing of port investments. Nevertheless, the federal government has adopted a policy that international financial organizations' loans are not in Russia's or its subjects' interest, and there is significant pressure to avoid them. In practice, however, international financial organizations continue to participate in the financing of the restructuring of the Russian port sector.

Environmental organizations are critical but lack influence

Russian environmental non-governmental organizations (NGOs) follow developments in the Russian port sector closely. In principle these organizations are very active and possess a high level of ecological and technological knowledge in the field. Russian legislation offers some channels for public participation in the decision-making of infrastructure projects such as the ports, especially at local and regional levels, such as public hearings.

Critically-oriented organizations in particular however continue to have difficulty in finding a platform for their concerns while decision-makers rarely cooperate with them. The main port sector -related strategic decisions are made at the federal level, in addition to major companies, and both these fields remain rather closed to challenges, monitoring and criticism from civil society.

The main instruments for the Russian environmental NGOs are lobbying through regional decision-makers sympathetic to a specific issue or NGO, making own investigations, producing or commissioning reports on particular issues and cases, working through media to draw attention to environmental issues, organizing seminars, bringing decisions of authorities to the court, collecting signatures for or against a specific issue, and demanding referendums.

Both success stories and failures as a result of these activities can be found.⁶⁵ However, public protests have not been successful especially if federal level decisions and authority have been at stake. For instance, utilizing an article in the Constitution, Russian environmentalists collected in autumn 2000 signatures in order to force a nation-wide referendum on (among other issues) the re-establishment of an independent federal agency for environmental protection in Russia. This was a reaction against President Putin's abolishment of the State Environmental Committee; its responsibilities were transferred to its traditional competitor and object of control, the Ministry for Natural Resources, where the Agency of Environmental Protection today has a status of one of the eight departments of the ministry.

This signature collection activity took place in 62 regions out of 89. Altogether over 2.5 million signatures were collected. However, as it turned out, the Central Election Commission, by citing numerous technical inaccuracies, deleted a considerable amount of the signatures collected, which left the environmentalists 200,000 signatures short of the 2 million needed to ensure the referendum.⁶⁶

Nevertheless, despite this failure the experience shows that civil society remains active in environmental questions, can engage public opinion, and might perhaps in some cases have real impact on environmental issues.⁶⁷ However, the critical public discussion about the environmental problems has become more difficult in recent years. True, the Kremlin adopted in 2001 a new approach towards civil society, aiming at mobilising the "constructive" part of the civil society more closely to public affairs. This resulted to high-level federal and regional "Civic Forums", where both the authorities and NGO activists gathered together, and finally to the establishment of the so-called Public Chamber in 2005. Also at regional level, authorities have started to cooperate with "constructive" NGOs in more systematic and institutionalized way, and both federal and regional legislation has been developed to this effect.⁶⁸

At the same time, the more critical NGOs, especially in the fields of ecology and human rights, who do not necessarily share the government's goals or methods, have started to experience harder times. For instance, FSB (the former KGB) representatives have often quite openly proclaimed that especially the environmental NGOs are representing rather foreign political, military or commercial interests and "espionage is carried out under cover of ecological organizations".⁶⁹

President Putin himself has encouraged this spirit. For instance, in July 2005 Putin made a statement⁷⁰ that "ecological expertise should not obstruct the development of the country and its economy", and accused foreign "partners", that is neighbouring countries, of funding Russian ecological organisations to slow down Russian port projects. "We have begun to

build a port close to Finland and I know as a fact that our partners [in foreign countries] have invested funds in the activities of environmental organizations, with the sole aim of obstructing the development of the project since it represents competition.” Putin told that he sees environmental challenges raised by foreign countries and Russian non-governmental organizations as an “attack strategy” by Russia’s competitors.

A major Russian environmental organization *Ecodefence* (*Ekozachtchita*) reacted to Putin’s statement by issuing a “serious warning” against a further weakening of environmental controls in Russia benefiting enterprises “close to government”. The organization’s spokesman said: “The head of state’s comments mean unequivocally that public ecological expertise may shortly be eliminated or transformed into a simplified procedure without participation of civil society”. According to him, “the Russian President fails to understand that there is a direct link between economic prosperity and the state of nature”.⁷¹

As to the port projects in particular, Russian environmentalists have been especially worried about oil spills both from the pipelines as well as from tankers. One might say that in the port sector the role of the environmental NGOs has been limited to expressing a critical voice. Nevertheless, their watchdog role is often very concrete and professional, based on making or commissioning much more critical “shadow” environmental impact assessments than the official ones.

For instance, when the Primorsk oil terminal was built in 2000 and connected to the the Baltic Pipeline System,⁷² Russian environmentalists maintained that environmental legislation about building the pipeline was not followed and, consequently, the risk of major accidents is high: “We did not find any waterproofing either on the pipe, nor, which is more important, on the welds. So the pipe corrosion has started even before its coming into use. The pipe’s wall thickness is about 8-10 mm. You can imagine how long it will last in such conditions, and the oil will be pumped through the pipes at 60 atmospheres pressure.”⁷³

Another typical example, illustrating the environmental NGOs’ very concrete monitoring role, is when in May 2006 a major oil slick with tens of tonnes of fuel oil was discovered in one of the local rivers in the Leningrad region, nearby town Vyborg and the Gulf of Finland. Also in this case environmentalists decided to make their own investigations, along the authorities: “The Vyborg district administration, *Baltnefteprovod* services, federal and municipal environmental services, and non-governmental environmentalists have examined the Baltic Pipeline System segment, and did not find any defects or leaks.”⁷⁴ Finally it turned out that the fuel in this case came from a nearby military units’ boiler.

Forestry industry

The development of Russia's forestry sector is especially important for those EU countries that have their own large industrial forestry sectors, such as Finland and Sweden. This is so for two reasons. First, the European wood processing industry imports round wood from Russia and the continuation and functioning of this import sector is regarded as crucial for the industry. Second, the European wood processing industry has started to invest in Russia and is willing to invest more if the circumstances are beneficial. In general, Russia is seen as a natural direction of development from the perspective of the European forestry industry.

Nevertheless, both goals are problematic when we consider the development strategies and practices of Russia's forestry sector. Therefore, this section reviews and discusses Russia's forestry sector's strategies, practices and network of actors especially from the two perspectives outlined above.

Russia's forestry sector strategy⁷⁵

Today, in most questions relating to the development of the forestry sector, at least at the highest political level, Russia's main strategy choices seem to be clear. Both the Kremlin's and the government's goal is that the sector should become self-sufficient in the medium to long term and should thus begin to contribute to the budget (through taxes, customs, forestry use fees etc.) in the same way as the energy sector, for instance. The main precondition for this is seen to be that Russia stops round wood export and instead becomes one of the main exporters of processed wood products in the world market. However, several challenges and unresolved questions remain before this goal can be materialized.

Russia's forest resources and their growth potential

Russia's forest resources are three times larger than those of Europe and its forest area is the largest in the world, constituting almost a fourth of all forest resources (809 Million *ha* compared to Brazil's 478 Million *ha*, Canada's 310 Million *ha*, and the USA's 303 Million *ha*). The growing stock has been estimated at 82,000 Million m³. However, this stock is unevenly located and only part of it can be easily and economically utilized because of the long distances and lack of infrastructure.⁷⁶ In principle, all of the forests around the railways have already been harvested while the forestry sector, in general, is not managed in a very sustainable and effective manner as compared to other major countries in the sector.

European Russia accounts for approximately 35% of the exploitable resource of Russia. Most of the forests are however located in Siberia or the Russian Far East in places with no proper means of communication. From the Northern-European point of view the most important area is Northwest Russia, with relatively easy availability in terms of the means of communication and with about 8063 Million m³ of growing stock. (See *Figure 7*)

Today the volume of the forestry sector is about 5 Billion USD, but in terms of optimistic Russian comments, particularly by politicians, it has been estimated that the future volume could be as much as 100 Billion USD, reaching almost the level of the oil, gas and metallurgy sectors in the production structure. For this to become reality, Russian experts have calculated that about 25 Billion USD should be invested into the Russian forestry industry by 2010.

These expectations are based on the potential for logging to increase, and on the possibility of working up the production degree as well as increasing demand in the domestic market. In respect of Western estimations these growth expectations are seen as unrealistic since they presuppose that almost all the growing stock could be utilized, which is seen as both physically impossible and economically unprofitable.

More realistic and professional Russian comments acknowledge that the potential growth figures are much smaller, but in any case, depending on the particular circumstances of the area, significant growth potential exists where the infrastructure links (roads, railway etc.) can be improved. According to the Federal Agency of Forestry Management of RF, today

the actual cutting down of forest comprises not more than 25% of the total (potential) calculated cutting volume or 50% of the calculated “economically accessible” cutting volume. Should this analysis be correct, it means that Russia could at least double its current cutting volume.⁷⁷ (See *Figure 7*)

To this effect, for the first time in recent years the Ministry of Transport put aside money for the improvement of forestry roads in its 2006 budget. The main problem here is that this approach would also presuppose enough investments be made in respect of creating new processing capacity if Russia is produce more than simply round wood for export.

Russian wood processing industry is dependent on foreign markets

In spite of its huge store of resources, Russia’s share of the world’s forestry industry product markets is about 2-3%. As to the forestry sector’s role in the Russian economy, it is the fifth largest sector in respect of GDP generated and the fourth largest in export terms.

Nevertheless, from the point of view of the sector’s relative share in terms of industrial production volume, GDP and export, in recent years it has been only a few per cent and thus it simply cannot compete with the gigantic oil, gas and metallurgy sectors.

In some parts of Russia the sector plays a more important role. For instance, in the Northwest federal district the forestry sector makes up about 15% of the whole economic structure. In some regions, such as Karelia and Arkhangelsk, it is the main economic sector with over 50% while for instance in Leningrad region its share is over 20%.

Over two thirds of the total production of the forestry sector is exported, which makes the sector rather depended on foreign markets. About one third of the export volume is in round wood, for which there is international demand, but which is not seen as beneficial to Russia in the long term. As to the more processed wood products, the problem is that Russian products are often not competitive enough in terms of price or that many of the processed wood products simply do not fulfil the quality or environmental standards demanded in the West.⁷⁸

The Russian forestry industry overcame a dramatic downturn in the 1990s, but started to recover after the August 1998 devaluation of the Russian rouble, which decreased the demand for imported forest-related products and gave an opportunity to increase output for the majority of Russian forest industry companies. Nevertheless, Russia’s forestry sector growth has been considerably slower than the average level of industrial growth in Russia in general and, as of today, it is not seen as very profitable business sector, though during the past two or three years growth has been somewhat stronger.

The locomotive for growth in the sector is the paper and pulp industry. The main bottlenecks however relate, in some products, to the inability of the primary production level to match the demand of proper raw materials, and in others, to the gap in production capacity in Russia which would make it possibly to cultivate all of the available raw material into processed products.

Recently the sector has however received a lot of attention from the government and it has also attracted investments from other sectors and from abroad. The reason why the federation is interested in the sector is that considerable expectations relating to future growth and thus to the importance of the sector are emerging. It has also become a kind of question of a national pride to the current Russian leadership that Russia, as the country of world’s largest forest resources, has to import a major part of its processed wood products instead of being a major exporter in the field.

After some failed attempts in the 1990s to reform the Russian forestry sector, in 2002 the Administration of the President and the federal government decided that a process of complete structural reform should be undertaken. This began as a more concentrated but longer-term vision and remains ongoing. It is however only from this point that we can speak of a Russian forestry policy, which eventually emerged from the mixture of laws and degrees, strategies, programmes and doctrines emanating from various different levels of the administration.

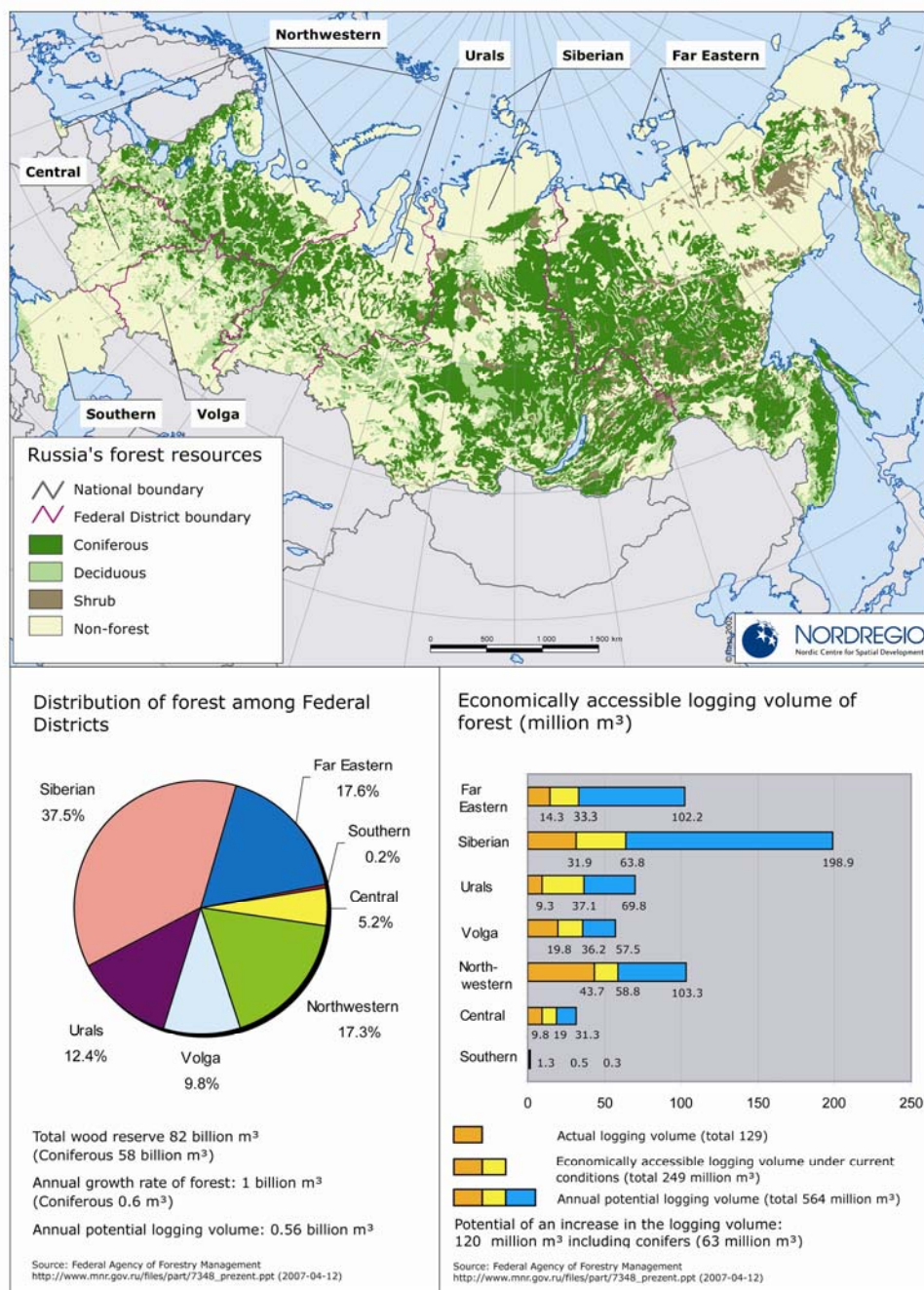


Figure 7: Russia's forest resources

Nevertheless, the forestry policy has not been easy to put together, reflecting the wider existence of bureaucratic and interest group struggles in Russia. In November 2002 the government accepted a document entitled *Basic development lines for Russia's forestry industry*, which was prepared by the (then) Ministry for Industry, Science and Technologies together with the Ministry for Economic Development and Trade. After that a Forestry Department under the Ministry of Natural Resources prepared a strategy paper entitled: *The development of Russia's forestry economy to 2010*, which the government accepted in January 2003.⁷⁹

While this document outlines the guidelines of forestry sector development, it was, however, subsequently contested by other similar documents. In addition, at the regional

level laws, degrees, strategies, programmes etc., exist reflecting the particular regional conditions. Thus, for instance, in the Northwest Russian federal district, the federal “super region”, has prepared forestry strategy papers specifically for that region.

These strategies make an effort to show the general prioritized direction of the forestry sector, the laws and decrees are supposed to put the goals into practice. Since 2005 a very complex and disputed process of drafting a new *Forestry Code* has taken place,⁸⁰ which from the beginning of 2007 replaced the previous *Forestry Code* from 1997 and the several amendments made to it between 1997 and 2007. The preparation of the new *Forestry Code* has been a complicated process, with several thousand proposals for amendments, put forward by different ministries, agencies, interest groups etc. Nevertheless, this new main law should put an end to the discussion over the basic elements of forestry sector reform and thus offer a more stable set of conditions for the future development of the sector.

From round wood export to paper and pulp⁸¹

The main challenge of the forestry sector, stated in every forestry-related speech of the President, ministers and other federal authorities, is to change the production and the export structure in particular so that instead of exporting round wood Russia produces and exports processed wood products, especially paper and pulp.

In doing this, the current ownership structure, where the forests are owned by the state (federation), will remain the main policy at least for the foreseeable future. (This, as such, is not unexpected since most of the world’s forestry resources, 84% on average, are publicly owned, though there are some regional differences.) At the same time, Russian forestry legislation and practice is to be harmonized with land legislation and practice such that a long-term renting of forests by private actors and the issuing of the corresponding licenses for their effective commercial utilization will become possible.

While previous legislation allowed 99-year renting rights the new *Forestry Code* has lowered this to 49 years. However, in practice the periods have so far been (and probably will continue to be) considerably shorter, at about 5 years and so, though during the last few years or so a tendency towards longer periods, of more than 10-years in some instances, can be identified. The long-term goal is that the forests, which receive long-term investment from private companies, could sooner or later be privatized.

The above-mentioned policy is supposed to lead to a more far-sighted forest use strategy, and to encourage the shift from exporting round wood to the creation of a forestry industry based on the processing of value-added products. A number of administrative measures are also to be used and have already been used to increase the level of processing, such as raising the export customs and tariffs on round wood; lowering or (partly removing) the taxation, export customs and tariffs on processed wood products and increasing the import costs respectively; as well as lowering the import costs of machinery for the paper and pulp industry.

The current policy of Russia, especially the raising of the export duties on round wood in early 2007,⁸² has become as a kind of surprise to many countries and foreign wood importing companies, although Russia has put forward its goals long before in its strategies. It has also become an issue between the EU and Russia, as the EU claims that Russia by its protectionist policy is not following their 2004 agreement about EU’s support to Russia’s WTO membership.⁸³

However, it remains to be seen whether the Russian policy will be successful or whether it has unintended consequences. The dilemma here is that while the strategy relies on the expectation of growing investments, it seems that the existing Russian forestry industry does not have sufficient capital to pay for large-scale re-development and the modernization of the wood processing industry, and, because of its relatively low profit margins, the sector has thus far at least been unable to attract enough of the necessary outside investment from other sectors or banks that would allow it to carry out its plans.

It has been pointed out that Russia has no factories that would use birch or aspen, for instance. Thus, the result might be that restricting or stopping the export of round wood does not lead to its use in domestic wood processing industry but that the timber will instead be left to rot in the forests, while the new administrative regulations will likely result only in driving the small harvesting companies out of business.⁸⁴ It is also probable that when the redistribution of Russia's forest resources, according to the new *Forestry Code*, has been finalised, the forestry oligarchs may start to see it to be in their self-interest to pressure the state to lower the export duties, depending on their own industrial processing capacity.

Actors and decision-making in the Russian forestry sector

Russia's forestry administration has been characterized by failed reforms, which have resulted into never-ending discussion and ill thought out reforms creating uncertainty about the rules of the game and the ownership structure of the industry. Currently, the main part of the forests themselves, as stated above, remain state-owned, but with the potential to be used by private actors within the context of a system of long-term rental arrangements. The forestry industry, in turn, has in general emerged as a rather oligarchic field after a rather turbulent period of privatization in the paper and pulp industries. The sector is also characterized by the existence of a considerable shadow economy and by numerous criminal activities.

The evolution of administrative reform⁸⁵

As in almost every other field the Administration of the President and/or the government both seek to coordinate the work between different bureaucracies and work as the decision-making forums for the most important strategic decisions in the forestry sector. Russia's forestry policy is written at the federation level, in the ministries and agencies dealing with the sector as well as in the state-owned or other research institutes close to the state administration.

Basically at least three ministries are involved, namely the Ministry of Natural Resources, The Ministry of Industry and Energy and the Ministry of Economic Development. The first is most closely connected to the forestry sector itself (forest administration and management), while the others deal with the industrial and trade-related parts of the sector. Clear-cut lines of division are, however, difficult to draw because of the constant administrative restructuring in the Russian bureaucracy.

The most important federal bureaucracy directly dealing with forests is currently, after a rather prolonged period of administrative reform, the Federal Agency of Forestry Management, which is subordinated to the Ministry of Natural Resources. Reflecting the general instability of the forestry sector administration in Russia, the future of the rather recently established Agency is however somewhat unclear. While at times there has been proposed that the effective development of the forestry sector would presuppose a ministerial level bureaucracy, in late 2006, on the contrary, speculation has emerged that the Agency should instead be abolished, because its duties can be taken care of at the regional level.

The regional level plays an important decision-making role in the forestry sector - though this is generally dependent on the specific political situation. While during the Soviet era, forests were administrated centrally from Moscow, at the beginning of 1990s their administration was decentralized and the regions received the right to manage the forests in terms of, for instance, deciding over the logging/renting rights – even if they were still owned by the federal state and in practice taken care of by state-owned forestry farms, or *leshovs*.

These rights were taken away again in 2004 and transferred to the federal level forest management. However, in 2005, connected to the larger administrative reform, which made the election of heads of the subjects (governors etc.) dependent on the support of the President, forestry management was again devolved back to the subjects; this was confirmed

by the new *Forestry Code*, which entered into force at the beginning of 2007. Basically this will give the subjects an important role in implementing the general guidelines for the forestry sector approved (and to be controlled) by the federal level.

Previously the forests deemed suitable for logging were forwarded to smaller districts, whose leaders then earmarked part of the incomes for the general budget and part of the logging areas were then divided according to special quotas between different special social groups, such as veterans for example.

According to the new *Forestry Code*, the system is to be such that the region will organise auctions in order to divide the logging areas. How this will work in practice is still (in early 2007) somewhat unclear, concerning, for instance, the question of who is entitled to participate in the auctions and under what conditions. In order to be effective the *Forestry Code* has to be synchronised with numerous governmental degrees. Most likely, based on earlier experience, the new law will also become a subject of several amendments in the coming years.

An oligarchic elite waging “forest wars”⁸⁶

As in other fields, the reasons for the current ownership structure of the Russian forestry sector can be found in the history of the 1990s. The first efforts to reform Russia’s forestry sector took place between 1991 and 1996. These badly prepared reforms resulted only in the fact that a considerable part of the forestry industry moved into the shadow economy, existing investment programmes were abolished and the export quotas were redistributed by criminal methods. Several directors of state-owned companies were later put on trial accused of stealing state property. Nevertheless, the largest existing wood processing mills (though not the forests) were privatized. During the process the forestry sector became one of the least transparent and most corrupt industrial sectors in Russia.

During the period between 1997 and 2001, the state was not actively interested in the development of the sector, which gave over the power of development over the rules of the game to the biggest companies in the industry. Often however these tacit rules included illegal methods, which resulted in ownership quarrels and hostile company takeovers, known in Russia as the “forest wars”. In principle, the question was about the struggle for ownership of the strategic parts of Russia’s forestry industry, based on the now privatized old Soviet companies. Other sectors, especially aluminium, oil and the banking sector, began however at this point to heavily interfere in the forestry sector which by now was seen as potentially profitable in the longer term.

While this process of restructuring remains ongoing, the “forest wars” basically led to the establishment of large privatized corporations in the same style as in the oil or metallurgy industries, occasionally either supported or countered by the interference of federal and regional authorities. At the same time the sector was nevertheless becoming somewhat more transparent as compared to the earlier shadow-economy like conditions, while it also became more far-sighted, the large corporations now looking not only at immediate profits but also concentrating on the establishment of long-term profitability.

This restructuring took the form of a reform of the forestry sector into so-called “vertically integrated” large corporations, which would have the resources to take care of the whole cycle of forestry, from logging to processing. Development in this direction was encouraged and welcomed especially by the federal authorities. As the sector became more organized with at least some, more or less, stable rules of the game, foreign investors also began to emerge onto the scene.

The further restructuring of Russia’s forestry sector is planned to be based on the existing wood processing sector and particularly on paper and pulp combines. This sector is largely controlled by private Russian companies or joint state-private companies while pure state companies remain few both in terms of production capacity and in number.

Most of the important forestry sector companies in Russia are active in Northwest Russia and they play an important role in the economic structure of the district. Of the 150 biggest

companies in Northwest Russia, about two dozen are connected to the forestry sector. Of Russia's eleven largest pulp factories seven are located in Northwest Russia and of the ten largest paper factories again, seven are in Northwest Russia.

Foreign investments welcomed – if the round wood stays in Russia

In its official policy, Russia welcomes foreign investment in the forestry sector if the goal is not to export round wood but to process the timber in Russia. And indeed, it has been argued that foreign investments is a necessity in the nascent Russian wood processing industry if it is supposed to be modernized and increase its role in the world market.⁸⁷

There are already several foreign forestry companies established in Russia, especially Northwest Russia, among them several Finnish companies. Direct foreign investment makes up the major part of foreign capital in Russia's forestry sector while a considerable part of this capital is in the form of loans from foreign banks. Only one or two per cent of all capital consists of portfolio investments.

However, while most European forestry companies simply import wood from Russia, and are often critically dependent on it,⁸⁸ even in those cases where some production capacity has been located in Russia it is mostly a question of Russian-based mills producing rather low value-added sawn timber to be further processed in the EU.⁸⁹

In practice foreign-owned companies face several problems, even if they would start to invest in more processed wood production. The biggest obstacle for foreign investments in the Russian forestry sector is the insufficient legal protection of foreign investments, in form of bilateral or multilateral investment protection agreements. The developments of the late 1990s and early 2000s showed that the use of the state apparatus as a weapon in the "forest wars" was widespread, which, naturally, is seen as a major risk of the foreign forestry industry planning to invest in Russia. Also the general turbulence of the domestic forestry-related legislation has hindered investment projects. For those foreign forestry enterprises, who invest in Russian forestry sectors (saw mills etc.) but base their investment strategy on the idea of exporting round wood or low value-added wood products from Russia, the Russian general strategy to prevent this (customs duties, administrative measures) has been naturally a major source of insecurity. In some cases foreign-owned companies face unfair competition conditions as well as contract problems which are difficult to solve fairly in arbitration trials. Finally, the idea that a foreign company utilises Russian forests is psychologically considered to be negative by the population and the local officials alike.

Widespread corruption and criminality

Corruption and criminality remain widespread especially in the primary production phase, i.e., the logging. In practice, the "original" price per cubic unit is often considerably underestimated compared to the market price paid by the forestry industry; the difference can be hundreds of per cent. The logging is done by small logging companies. They then sell the round wood to either Russian or foreign markets and share their profits with the local authorities. In this kind of system, those authorities involved in the logging business are not interested in restructuring or reforming the forestry sector because of the short-term benefits they currently enjoy.

Furthermore, illegal logging remains a major problem in Russia. The volume of the illegal logging is calculated to compose 10-15% of the total volume of logging, which annually would mean about 19 Million m³. In 2005, the annual value of the illegal logging was estimated to come up to 180 million USD.⁹⁰

This systematic and large-scale organised crime takes place either in connection with legal logging by falsifying documents and in that way enlarging the area to be felled or it takes place directly via illicit criminal groupings. Most part of this round wood is supposedly used in the sawn timber industry within the shadow economy, since official statistics show that the domestic market would have diminished over the last ten years by almost two hundred and fifty per cent, something that has not occurred. Corruption in the authorities who, for

instance, control transport or whose passivity enables the criminal logging to continue is a precondition for this activity. Since this system however also provides benefits to all involved it is hard to stop. It is acknowledged by Russian authorities that also Russian wood export involve a considerable amount of illegally felled timber.⁹¹

As to the illegal logging, one cannot yet speak about a national or regional “forestry mafia”; however, it is rather a question of rather small criminal groupings that have connections to the local authorities and to the state forestry farms.

In some regions special groups have been established to combat this type of criminality. Earlier the prosecution of this type of organised crime was not prioritised by the authorities, but in recent years much more attention has been paid to the problem from the very highest level of the federal administration. Satellite technology was introduced in 2005 as an instrument to monitor and control part of the forest areas and the system is supposed to be extended to cover all areas by 2007-08.⁹²

Competing interest organizations

A number of interest organizations represent the various parts of the forestry sector such as, for example, the Union of Timber Manufacturers and Exporters of Russia (UTMER) have emerged. Recently however the Federal Agency of Forest Management has bemoaned the fact that Russia lacks a united and strong forestry sector interest organization which makes the development of the forestry sector more difficult. Therefore it has suggested that a Confederation of the Unions of Harvesting, Pulp and Paper Industry, and Wood and Furniture Industries should be established. This kind of confederation was actually established in accordance with the recommendations of the Agency, at least on the paper. It is likely however that even under these conditions competing interest organizations representing different financial and industrial groupings will continue to exist.

Russian environmental organizations have traditionally been particularly interested in forestry protection adopting a highly professional approach to lobbying for conservation in the field. While the general situation of Russian civil society-state relations was briefly pictured in the end of the port sector section, the role of environmental NGOs in the forestry sector is however somewhat different to that of the environmental NGOs for instance in the port sector. This comes from the fact that the environmental NGOs here focus in their criticism and monitoring efforts on the same issues as the federal authorities, namely corruption and the illegal utilisation of the forests. Their role is also one of putting forward new ideas related to the sustainable development of the forestry sector in Russia. Thus, in principle, the environmental organizations may and do collaborate with federal forest authorities. This, however, often brings them into conflict with the regional or local authorities involved in the sector.

4. Conclusions and implications

The above discussion aimed at showing that Russia's policy in respect of European integration is characterized by a combination of integrationist and protectionist impulses. The reviews of the three industrial sectors in Russia, that is, international road transport, ports, and the forestry sector, illustrate how the basic situation appears somewhat different depending on the particular sector involved.

This concluding section begins by briefly summarizing how Russia's policies in respect of integration and protectionism appear in the sectors under review. After that, the implications for the EU, its Member States and enterprises are outlined.

Diverse forms of integration and protectionism

One can conclude that in respect of general Russian policies in the sectors reviewed above, the geopolitical model presented in the beginning of the report is, in most cases, sufficient to explain Russia's strategic choices. Each of these sectors are from the Russian point of view strategically important economic areas, since they are related to transport or raw material export; thus, in the context of current Russian thinking they are closely linked to the state's national interests and security.

The general goal of the Russian state is to modernise these sectors, which presupposes enhanced international cooperation and often foreign investments. At the same time, the Russian state wants to protect these fields of economic activity from foreign competition as much as possible and at the same time attempt to keep them in one way or another under state control. From the geopolitical perspective, Russia's strategies in each of the fields, combining integrative and protectionist features, appear rather rational.

Nevertheless, the geoeconomic approach, focusing on conflicting interests within Russia and seeing Russia's policies more as a result of elite bargaining and compromises than of any geopolitical master plan, helps us to appreciate the complexity of concrete situations and actor networks. In this way perhaps Russia's often contradictory behaviour becomes a little more understandable.

The main features of the three sectors dealt with in this report, and the related main resultant problems for the EU, its Member States and EU-based enterprises, are summarized in *Table 5*. In the context of international road transport, Russia's strategic goal is to become a transport link between Europe and Asia. Thus, Russia is clearly aiming at closer integration with the outside world. The most obvious challenge for the materialization of this goal is the need for an extensive and necessarily expensive modernization of the main highway networks.

Protectionist policies express themselves in this field in that at the same time the Russian state has given itself the task of defending Russian transport enterprises from foreign competition. This protectionism sometimes takes the form of arbitrary discrimination and decisions as well as violations of previously agreed rules.

The dilemma here is that while protectionism seems to serve the interests of Russian truck transport enterprises, it seems less likely that it will help in the Russian state's strategic goal of becoming a transport corridor between Europe and Asia. It is doubtful that other countries will simply give Russia that position, if it is to be only Russian trucks driving through that corridor. Protectionism only tends to isolate Russia from international transport routes.

Table 5 International road transport, ports, and the forestry sector in Russia: A summary				
Sector	Russia's strategic goals	Main challenges (from the Russian point of view)	Main features	Main problems for the EU, the Member States and EU-based enterprises
International truck transport	Russia as a transport link between Europe and Asia	Modernizing the main highway network Defending Russian transport enterprises from foreign competition Modernizing the trucks in accordance with European environmental standards Simplifying the cross-border bureaucracy	The state defines the strategic goals, the federation is main decision-maker Institutionalised cooperation between the main interest organization and Russian state authorities Fragmented ownership structure with tens of thousands of small, medium and large-scale private companies, some state-owned companies still left A tendency towards a more transparent but centralized ownership structure Shadow economy, corruption and criminality widespread	Protectionism, which sometimes takes the form of discrimination, arbitrary decisions, and violation of previously agreed-upon rules Russian cross-border bureaucracy, which creates huge truck queues at the border (on both sides), disturbing both the truck enterprises and their drivers, companies using their services, as well as other traffic Organized crime (connected to corruption), threatening the safety of road transport
Ports	Self-sufficiency in port capacity	Diversifying the port capacity so that Russian ports could not only handle oil and raw materials but also value-added products in containers	The state defines the strategic goals, the federation together with large export companies (oil and raw materials) main decision-makers when deciding about port build up Ports owned by large export companies, with minority state shares (small part of the infrastructure)	Finnish and Baltic States' ports face growing competition from the Russian ports Environmental concerns, especially increasing probability of large-scale oil spills in the Baltic Sea as the Russian oil exports increase

Forestry	Moving from round wood exporter to a major pulp, paper and other processed wood products exporter in the world market	Need for large-scale investments in new factories and machinery The absence or bad condition of forest related infrastructure (roads, railway etc.) Long distances and problematic location of the forests Illegal logging	<i>Forests:</i> The state defines the strategic goals The federation owns the forests and defines the rules of the game, but regions administrate them. Long-term renting of forests up to 49 years possible for private companies <i>Forestry industry:</i> A tendency towards “vertically integrated” large corporations, which would have the resources to take care of the whole cycle of forestry, from logging to processing	The European forestry industry’s strategy, which is based on importing round wood or low value-added wood products from Russia, is facing problems as Russia limits round wood export by raising customs duties and by other administrative measures The biggest obstacle for foreign investments in the Russian forestry sector is the insufficient level of legal protection afforded to foreign investments, in the form of bilateral or multilateral investment protection agreements. Also the general turbulence of the domestic forestry-related legislation has hindered investment projects. In some cases foreign-owned companies face unfair competition conditions as well as contract problems which are difficult to solve fairly in arbitration trials. For those foreign forestry enterprises, who invest in the Russian forestry sectors (saw mills etc.) but base their investment strategy on the idea of exporting round wood or low value-added wood products from Russia, the Russian general strategy to prevent this (customs duties, administrative measures) is naturally a major source of insecurity. Finally, the idea that a foreign company utilises Russian forests is psychologically considered to be negative by the population and the local officials alike.
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The port sector is, in principle, all about integration with the outside world and with the world economy, as it is directly and physically related to Russia's foreign trade. Moreover, this trade is rapidly increasing and also becoming more diversified. This does not however sit well with basic Russian state ideology, which is to avoid interdependencies between Russia and its neighbours when it comes to Russian foreign trade routes, and thus to rely as much as possible on Russian ports.

Thus, Russia's ongoing build-up of the port sector is clearly related to the Russian state's great power logic preserving sovereignty and autonomy in this strategically important field. This, as is the case in international road transport, clearly contradicts Russia's declaratory policy position of becoming more closely integrated into Europe and into the world economy. It might however also be, at least in some cases, economically rational to build new ports from the perspective of the large export companies and the particular regions where the ports are located.

In the forestry sector, Russia is unhappy with its role in the current international distribution of labour. Russia's strategic goal is to progress from round wood exporter to a major pulp, paper and other processed wood products exporter in the world market. To this effect Russia is rapidly raising round wood export duties.

It is however unclear as to whether this policy is actually beneficial to anyone. The result might be that the forestry sector loses a significant amount of income while the wood cannot be utilized in domestic production. Russia does not moreover seem to be particularly active in creating legal and other preconditions for increasing foreign direct investment in its forestry sector although such investments are demanded and welcomed by the highest political-administrative elites.

Implications for the EU, the Member States and EU-based enterprises

Given the current situation, what then would be the best strategies for the EU, its Member States and EU-based enterprises in dealing with Russia? Here it is proposed to distinguish between three levels and/or types of strategies, all currently though in different combinations, present in EU-Russian relations. Each of the strategies could however be considerably intensified.

The first, entitled the *integration strategy*, is to be utilised at the EU-Russian level of negotiations, and would be based on the normative long-term goal of improving and deepening the EU-Russian partnership, particularly in the field of trade and economic integration. Thus, the question here concerns the need to go beyond the current rather obscure and vague CES formula, making the priority goal a free trade area agreement, and thereafter a single market with a clear-cut plan and schedule. This strategy, if followed, would basically in the longer term solve most of the trade conflicts currently characteristic of EU-Russian relations.

The second, the *problem-solving strategy*, calls for the intensified defence of the EU/Member States/enterprises sectoral and functional interests, particularly in respect of problems arising from Russian protectionism, discrimination or violation of commonly agreed upon norms and rules. What is needed here is not bilateral solutions between individual Member States and Russia, but rather an effective EU-level mechanism, which would automatically introduce symmetrical sanctions against Russia, when it makes politically motivated moves in its trade policy against a Member State, or when its foreign trade and other bureaucracies impose such rules or sanctions on EU-based enterprises, which clearly violate previously agreed-upon rules.

The third strategy, here characterised as the *adaptation strategy*, is best suited to the sectoral and company level. It calls for enterprises to make the best of the current situation by adapting to current Russian circumstances as closely as possible, while waiting for Russia to

become more deeply integrated into Europe and more accepting of the respective norms, rules and behavioural patterns.

This report concludes by briefly describing and discussing these three strategies, which are summarized in [Table 6](#).

Integration strategy

The EU's opinion is that the problem of non-functioning or at least static EU-Russian relations is not so much in the current approach but in Russia's current political development. In a rather straightforward style, the EU's *Country Strategy Paper 2007-2013, Russian Federation*, states as follows:

“Given current political and economic circumstances, the EU will need to work hard to maintain the pressure for the implementation of the Common Spaces. Russia is characterized by a powerful bureaucracy, a politically-biased legal system, powerful and repressive law enforcement agencies and a relatively weak civil society. Power is increasingly concentrated within the Presidential administration.”⁹³

However, what if the problem lies, at least partially, in the fact that the Common Spaces, including the CES, are in their current form neither effective nor motivating enough? It seems clear however that the current CES approach cannot provide any tangible framework solutions for EU-Russian economic relations. The current CES with its *Road Map*, being actually a list of priorities rather than any road map, is lacking two things in particular: a clear-cut *goal* and a *schedule*. In order to go beyond the current approach, something similar to the strategy proposed here should be discussed and detailed between the EU and Russia. (See [Table 7](#))

The first stage would be to detail the CES so that a clear goal of a FTA, followed by a single market would be articulated. While Russia joining the WTO should be regarded as a natural starting point for preparatory discussions on the preconditions of a FTA, the goals of a FTA and a single market should also be included into the new or amended PCA (the current agreement expires in December 2007).

During the preparatory phase, Russia's voluntary approximation of relevant legislation closer to that of the EU would be necessary in order to create a minimal regulatory basis for the FTA. This would, however, be a natural follow-up to the WTO negotiations, and should not create much opposition from the Russian side.

Before, or immediately after, beginning the factual negotiations, the specific question on the principles of how the partial post-Soviet Commonwealth of Independent States (or Single Economic Space) integration, aimed at a functioning customs union, could be connected to an EU-Russia FTA, should be solved. Moreover, to be realistic, the FTA should be rather flexible with sectoral transitional periods safeguarding both the EU and Russian short-term interests.

Similarly, the single market negotiations could be started with preparatory discussions on the necessary preconditions, in particular defining the necessary level of legal approximation. At this phase, one should consider whether it would be possible and acceptable for both parties to create an institutionalized mechanism in respect of how Russia would automatically approximate its legislation to that of the EU in the relevant spheres, *perhaps* including a system where the EU consults Russia in the preparatory phases of the legislative processes concerning single market legislation, giving Russia the ability to make comments and proposals. Consensus agreements so achieved would be automatically and voluntarily proposed or included in the relevant Russian legislation.

The legal approximation question would basically define the nature of the EU-Russia single market regime, namely whether it would resemble some existing bilateral (Switzerland) or multilateral (EEA) solution, or whether a new model should be created. In any case, the

goal should be an EU-Russia single market regime (with sectoral transitional periods), which would enable Russia to participate in most fields of the EU Common Market by 2020. More difficult questions, such as the degree of labour market or service market integration/liberalisation could however be solved after this deadline.

Problem-solving strategy

Current EU-Russian relations, including the CES, are, as argued throughout this report, in fact based on a rather unambiguous problem-solving approach. The main ideology here is to deepen the level of cooperation within some functional and sectoral fields (see *Table 2*), but actually the work is pretty much concentrated on reactive (and sometimes preventive) problem solving rather than on creating new, deeper levels of integration.

This kind of approach as such is needed (though it is not enough). In many cases, the essence of this approach is the EU's reaction to problems arising from Russian protectionism, discrimination or the violation of commonly agreed upon norms and rules.

The problem here seems to be that problem solving is not functioning very well from the EU's point of view. The nine Sub-Committees⁹⁴, mentioned in the PCA, do not resolve or even deal with any real problems, and often there are long periods when they do not meet at all. The specific "dialogues", be they in the field of energy or transport, do not in practice moreover even attempt to resolve any of the major problems between the EU and Russia. The different working groups around the CES in addition to the above-mentioned ones do not do any better.

This has led to a situation where two possibilities exist. The first is that the Member States are left alone to sort out their problems with Russia. Bilateral negotiations with Russia are, however, difficult, because any Member State, at least the smaller ones, rarely have enough tools to pressure Russia. For instance Finland has experienced this concretely in its road transport relations with Russia.

The second possibility is that the EU defines the problem as not bilateral but as "European". This usually takes place only after a considerable and prolonged bilateral conflict. In this case however the only level where the EU can more or less effectively deal with the problems, often initiated by some Russian middle-level bureaucracies, is the highest Commissioner (EU)/ministerial (RF) level discussions.

A case in point here is the (in early April 2007) 17-month-old Russian ban on Polish meat and plant product imports. At the beginning of the crisis, Poland asked for the EU to pressure Russia and take up counter sanctions. Only after Poland vetoed the commencement of EU-Russian negotiations on the new PCA (as the present one is coming to its end) did the EU however come to define the issue as a "European" one by taking the issue up at the highest political level. The EU could not quickly find a solution with Russia even then though it did not threaten Russia with sanctions.

The lesson here is surely that the EU's problem-solving approach does not work with Russia to the benefit of the Member States. The difficult issues are hard to solve bilaterally, they become even harder when they are prolonged, while by the time they are addressed at EU-Russian political level they have already been politicized and a lot of face saving is necessary.

Yet an effective solution could have been to impose, without delay, symmetrical joint EU trade sanctions on Russia, making perhaps illogical linkages between issue areas in the same way as Russia does.

Thus, while the integration strategy must be based on a patient search for the best possible long-term solution, the problem-solving strategy should be based on backing the negotiations with the potentiality of sanctions. If this would be done automatically at the middle-level of European Commission bureaucracy, the issues would not necessarily become so politicized.

This automatic solidarity and reactive practice would also, after a while, have the likely effect of preventing Russian bureaucracies from taking arbitrary decisions and violating previously agreed upon rules, because such decisions would become too costly.

Adaptation strategy

The adaptation strategy is best suited to the sectoral and company level, although individual companies may also benefit from the actions taken by the EU and/or Member States. Given the problems with regard to Russia, such as protectionist legislation, companies might decide to avoid or withdraw from Russian markets while waiting for Russia to become more closely integrated into Europe, and to adopt its norms, rules and practices. Instead, the best alternative might be just to study the current Russian circumstances as carefully as possible and then to try to better adapt to these circumstances.

This might best be illustrated with reference to the forestry sector, for instance, on the basis of the sectoral analysis above. Russia's forestry strategy is based on the idea of changing its production and the export structure such that instead of exporting round wood Russia produces and exports processed wood products, especially pulp and paper but also furniture, building materials and the like. Therefore, should the European forestry industry want to continue to have access to Russian forests for raw materials, it should consider moving its production to Russia or investing there. In so doing, European forestry enterprises should follow Russian practices, namely creating (or becoming a part of) "vertically integrated" large corporations, which would take care of the whole cycle of forestry, from logging to processing. This would mean that the European forestry industry should participate in the redistribution of Russian forest resources. This solution would probably be acceptable to the Russian state, while it would make the foreign companies concerned less vulnerable to disturbances in one part of the production cycle. As the question concerns large levels of investment however, the EU level (integration strategy) should also be used along with bilateral arrangements to secure the protection of these investments.

Similarly, in the port sector Russia's strategy is clearly formulated as aiming at self-sufficiency. This is however not something that the EU could or should legally (or morally) resist, even if Russian policy is not always based on rational economic calculations but rather on great power interests. It seems clear however that if the Finnish or Baltic ports want to be successful in competing with Russia over the increasing flow of goods to and from Russia, they need to find their own *niches* in this competition environment and in particular adapt their strategies to the capacities and future perspectives of Russian ports.

For instance, it was pointed out in the text above that it will take until around 2015 before Russia has sufficiently increased its port capacity in terms of the type of infrastructure needed to be able to successfully address the growing transport volume in container traffic. This gives the Finnish and the Baltic States' ports at least an eight year window of opportunity to adapt to the envisaged market changes. One could also find other spheres of port transport where Russian ports cannot compete, at least for the time being. Moreover, one can compete with efficiency and flexibility, for instance, offering quick service, a variety of technical equipment, safe depots, links to other versatile transport infrastructures (railway and road networks) and so forth. At least for the time being then, as these features are not the strongest elements of the Russian port infrastructure, Finnish and Baltic ports should be able to successfully compete.

In international road transport, the adaptation strategy again means taking advantage of the existing possibilities to avoid Russian administrative and other measures aimed at protecting Russian truck enterprises. It might then be rational for more foreign truck enterprises to follow the example of those pioneers who have established affiliated companies or offices, which are registered in Russia, in order to avoid protectionist regulations.

Table 6 Implications for the EU, Member States and EU-based companies		
Different strategy levels	Current approach	Proposed intensified approach
Integration strategy	PCA CES as a list of priorities	New PCA and CES with a clear-cut goal (free trade area, single market) and respective schedule (see <i>Table 7</i>)
Problem-solving strategy	PCA committees and Sub-committees, CES working groups and “dialogues”, mainly for information sharing High-level consultations for problem solving, politicizing the issues, usually no sanctions. Member States often left alone to deal with concrete practical cooperation problems.	Creating an effective EU mechanism (middle-level), which would automatically introduce symmetrical sanctions against Russia, when Russia makes politically motivated moves in its trade policy against a Member State, or when its foreign trade and other bureaucracies impose such rules or sanctions on EU-based enterprises, which clearly violate previously agreed-upon rules.
Adaptation strategy	Adapting partially to Russian markets but often with expectations that conditions in Russia can be faced with similar company strategies as in more liberal market conditions. Avoiding or withdrawing from Russian markets because of protectionist obstacles and insecurities.	To study the current Russian circumstances as carefully as possible, trying to adapt to these circumstances. This might include: - competing with Russian enterprises with efficiency, flexibility, special knowledge or equipment - creating affiliated offices, registered in Russia, in order to avoid protectionism and discrimination - moving production to Russia - trying to control the whole cycle of the field of economic activity, avoiding externalization of parts of important elements. For instance, in forestry, a foreign company should control the activities from logging to processing and transport

Table 7 EU-Russian economic integration up to 2020: An intensified approach	
(2005)	(Starting to implement the Road Maps for the Four Common Spaces, including the CES Road Map)
2007	Clarifying the goal of the CES as leading first to a free trade area and after that to a single market (multilateral “Russia-EEA” or bilateral CES) Russia’s WTO membership Starting preparatory discussions on the free trade area Finishing negotiations on the new, or amended, PCA including the goals of a free trade area and a single market Russia’s voluntary approximation of the relevant legislation closer to that of the EU in order to create a minimal regulatory basis for a free trade area Starting negotiations on a EU-Russia free trade area Including a solution to the question of how the CIS (or SES) integration, aiming at customs union, could be connected to the EU-Russia free trade area
2010	Starting negotiations on a visa free regime Finalizing the negotiations on and ratification of the free trade agreement With sectoral transitional periods Starting preparatory discussions on the conditions for a single market Goods, services, capital, partial free labour movement Defining the necessary level of legal approximation Creating an institutionalized mechanism of how Russia would automatically approximate its legislation to that of the EU in the single market related fields, based, for instance, on the following principles: Russia’s voluntary approximation of its legislation to the existing single market related EU legislation EU consulting Russia in the preparatory phases of legislative process concerning new single market legislation, giving Russia the ability to comment and make proposals Consensus agreements so reached would be voluntarily included in Russian legislation
2015	Starting negotiations on a EU-Russia single market Finalizing the single market agreement Either as multilateral “Russia-EEA” agreement or bilateral CES agreement With sectoral transition periods
2020	The single market agreement ratified and comes into force

Notes:

A reference to a website below is based on its availability in March/April 2007.

¹ Elements of particularly the following papers have been included in this report: Christer Pursiainen, *Theories of Integration and the Limits of EU-Russian Relations*, International Studies Association Convention 2007, Chicago, USA, 1 March 2007, to be found at <http://archive.allacademic.com/one/isa/isa07/index.php?cmd=isa07>; Christer Pursiainen, "Road Maps", in Christer Pursiainen and Sergei Medvedev (eds.), *Towards the Kaliningrad Partnership in EU-Russian Relations: A Road Map into the Future*, Moscow: Recept 2005.

² There are, of course, more than these two approaches that can be used in analysing EU-Russian integration. For a comprehensive overview of the alternative theories, see Pursiainen 2007, *op. cit.*

³ This approach is basically based on a combination of different types of realism or Realpolitik, cf. Pursiainen 2007, *op. cit.*

⁴ Kari Liuhto, *A future role of foreign firms in Russia's strategic industries*, Electronic Publications of Pan-European Institute 4/2007, Turku School of Economics, to be found at http://www.tukkk.fi/pei/verkkajulkaisut/Liuhto_42007.pdf

⁵ Iver B. Neuman, "Russia as a great power", in Jakob Hedenskog, Vilhelm Konnander, Bertil Nygren, Ingmar Oldberg and Christer Pursiainen (eds.), *Russia as a Great Power. Dimensions of Security Under Putin*, UK: Routledge, 2005, pp. 13-28.

⁶ When it comes to EU-Russian trade, the same structure prevails. The EU's exports to Russia, as of 2005, included machinery (36%), chemicals (14%), manufactured goods (classified chiefly by material [11%], transport equipment [10%], food and live animals [7%]). Russian exports to the EU consisted mainly of energy or mineral fuels (65%). Exports also include manufactured goods (9%), primary products (6%), crude materials except fuels (4%), and chemicals (3%). See

http://ec.europa.eu/trade/issues/bilateral/countries/russia/index_en.htm There is also another imbalance, namely the EU is overwhelmingly Russia's main trade partner, accounting for over half of Russia's foreign trade, whereas Russia's share of the EU's external trade remains clearly under ten per cent. In other words, the EU is much more important for Russian foreign trade than *vice versa*. Nevertheless, the EU is very much dependent on Russian gas, and for some Member States, such as Finland, Russia is the main foreign trade partner. In the EU's *Country Strategy Paper 2007-2013, Russian Federation*, the development of the EU-Russian trade relations are characterised shortly as follows: "Russia is a large commodity exporter and has benefited from favourable terms of trade since 2000. The EU is easily Russia's most important trading partner (followed by the CIS countries and China), while Russia is the EU's fourth most important partner. Russia enjoyed a trade surplus of some €35 billion with the EU in 2004. The EU's most important export to Russia is machinery. The EU is also the main source of technology, know-how and investment for Russia. In turn, Russia has immense natural resources and a qualified labour force. Still, the structure of Russian exports is rather unbalanced and largely dominated by mineral fuels and raw materials. Other export sectors are chemicals, agriculture and industrial products. Over the past few years, EU-Russian bilateral trade has grown by more than 10% Given that the majority of the new EU Member States are traditional economic partners of Russia, this trend is likely to be maintained. Examination of monthly figures for the 1995-2005 period reveals that by mid-2005 the EU-25 received close to 60% of all Russia's exports, a notable increase from the roughly 45% of the mid-1990s, and supplied 44% of Russian imports. Yet Russian imports from the EU fell in share terms by more than 10%, from the 55% observed in the mid-1990s: close to half of this loss can be related to China's growing importance in world markets, as this country quadrupled its share of Russian imports, from 2% to around

8% over the period in question. This fall in the EU share in Russian imports was not affected by the 2004 enlargement [...].” See Section “6.9. Thematic programmes”/”Economy”/”Trade” (p. 34,35), to be found at http://ec.europa.eu/comm/external_relations/russia/csp/2007-2013_en.pdf

⁷ These were the “goals of integration” that Paul Streeten, one of those economists looking at the European integration from this perspective early on, defined in 1961; see Paul Streeten, *Economic Integration. Aspects and Problems*, Leyden: AW Sythoff 1961.

⁸ In Pursiainen 2007, *op. cit.*, this approach is discussed in more detail, distinguishing between different variations of Marxist theories on integration and more “neutral” International Political Economy approaches (IPE). For an overview of the different Marxist approaches, see Colin Shaw, *Reconsidering the relevance of Marxist state theories to European integration*, Paper to be delivered to EPSNet Conference, Prague, June 2004, to be found at <http://www.epsnet.org/2004/pps/Shaw.pdf>; see also, for instance, Peter Cocks, “Towards a Marxist Theory of European Integration”, *International Organization*, Vol. 34, No. 1 (Winter, 1980), pp. 1-40; Kees Van der Pijl, *Transnational Classes and International Relations*, London: Routledge 1998. For a representative example of non-Marxist approaches in the IPE, see, for instance, the work of Wayne Sandholtz at <http://www.faculty.uci.edu/scripts/UCIFacultyProfiles/DetailDept.CFM?ID=2935>; see also John Zysman and Andrew Schwartz (eds.), *Enlarging Europe: The Industrial Foundations of a New Political Reality*, University of California Press: University of California 1998.

⁹ See *Business elites and Russian Foreign Policy*, Russia Beyond 2000, 5(2000), Finnish Institute of International Affairs, Helsinki 2000, co-edited by Anisa Doty, Tuomas Forsberg and Christer Pursiainen on the basis of Sergey Medvedev (ed.) larger work. The report looks at some key industrial sectors and their interests *vis-à-vis* the EU. Beginning with the *gas sector*, it concludes that the sector is a major advocate of developing good relations with Europe based on long-term strategic interests and interdependence. Nevertheless, conflicts with the general integrationist goal are possible over issues relating to the regulatory role of the Russian state especially concerning domestic energy prices, the industry’s own monopolised structure which it does not want to be challenged. The Russian *oil industry* is also supportive of closer ties with Europe, particularly as this will create conditions to attract western investment and capital, though within the limits of the Russian state’s “strategic interests” of preserving its control over the industry. However, in terms of future target markets, the industry’s strategic priorities lie mainly in Asia and the USA, which also may reflect Russia’s policy towards Europe. The *electrical power industry* is also in favour of Russia’s integration into Europe, seeing Europe (and especially the neighbouring EU countries) as potential markets for electricity produced in Russia. As to the nuclear industry in particular, the industry’s elite is divided between traditionalists who remain nostalgic for state control and a more reformist group already reconciled to the market and thus more supportive of an open economy. The nuclear industry would like to gain access to European markets but is hindered by trade barriers, the loss of position in Eastern Europe, and negative public attitudes in Europe towards nuclear power and particularly the Russian nuclear industry. The *metal industry* also advocates continued international openness and integration with Europe. During the 1990s this industry became one of the most export-oriented industrial branches in Russia, exporting over half of its total output. Increased cooperation with the EU is essential for the prosperity of this branch, and one of the industry’s main problems concerns EU protectionism, not how to protect itself by domestic protectionism. The *defence industry* has a rather nationalistic orientation. It is divided between those who long for a return to Soviet times, with regular state defence orders and privileged status, and those who recognise market realities and try to cooperate with the West. On the whole, this industry is not a major advocate of expanding relations with the EU although ideological nostalgia for Russia’s lost superpower role is gradually giving way to a more pragmatic search for partners across the globe. Nevertheless, in trying to increase its market share, Europe’s role is viewed

more as that of a competitor than as a partner, as the foreign markets for Russian defence industry lie mainly in Asia and Africa.

¹⁰ Peter Vahtra & Kari Liuhto, *Expansion or exodus? – Foreign operations of Russia's largest corporations*, Electronic Publications of Pan-European institute 8/2004, Turku School of Economics and Business Administration, to be found at http://www.tukkk.fi/pei/verkkojulkaisut/Vahtra_Liuhto_82004.pdf. See also Kari Liuhto (2002a), *The internationalisation boom of Russian corporations – Studies of Russian Banks, Energy and Metal Companies*, Research Report N:o 135 2002, Lappeenranta University of Technology.

¹¹ Russia consists of 49 regions (oblasts), 21 republics, 10 autonomous districts (okrugs), 6 territories (krays), 2 federal cities (Moscow and Saint Petersburg) and 1 autonomous region (oblast). Altogether it makes 89 federal administrative units of the Russian Federation.

Hereafter all of these 89 territorial and administrative entities are referred to as “regions”.

Should we look at Russia's integration into world economy and the EU from this perspective, we can find the following quotation, for instance, from an analysis dealing with the impact of Russia's forthcoming WTO membership: “There are parts of European Russia close to markets of Western Europe and Far Eastern Russia that is close to the markets of China and Japan, while large portions of Siberia are relatively isolated. We can expect the impacts across the regions to be very diverse, even for the same industry. Consequently, there is a need for a model of Russia that distinguishes the regions of Russia.” See Thomas Rutherford and David Tarr, “Regional Impacts of Russia's Accession to the WTO”, to be found at http://siteresources.worldbank.org/INTRANETTRADE/Resources/Internal-Training/287823-1116536061368/Regional_ImpactsOfRussiasAccessionToTheWTO.pdf

¹² There are a lot of macroeconomic and sectoral (aluminium industry, banking etc.) analyses on the theme “Russia and WTO”, see, for instance: the World Bank analyses to be found at <http://web.worldbank.org/WBSITE/EXTERNAL/TOPICS/TRADE/0,,contentMDK:20273889~menuPK:207652~pagePK:148956~piPK:216618~theSitePK:239071,00.html>; the analyses at the “Russian” official WTO web site <http://www.wto.ru/documents.asp?f=docs&t=14>.

¹³ For the chronology of Russia's negotiations, see http://www.wto.org/english/thewto_e/acc_e/a1_russie_e.htm

¹⁴ According to a summary of an international seminar on the theme in 2003, to be found at <http://www.carnegieendowment.org/events/index.cfm?fa=eventDetail&id=620&>

¹⁵ Anders Åslund, “Russia's WTO Accession”, Testimony at the Hearing on EU Economic and Trade Relations with Russia, Committee on International Trade, European Parliament, Brussels, November 21, 2006, to be found at <http://www.iie.com/publications/print.cfm?doc=pub&ResearchID=686>

¹⁶ Quoted from the official Russian government related WTO website <http://www.wto.ru/russia.asp?f=target&t=9>

¹⁷ Åslund 2006, *op. cit.* Anders Åslund, one of the main analysts and former “foreign insiders” of Russian economic policy decision-making, argues that the positive effects on the Russian economy from WTO accession would be substantial and beneficial also for the EU. He estimates “that Russian total two-way trade in manufactures could double from \$187 billion (in 2005) to \$352 billion. As the European Union is by far Russia's biggest trade partner, the European Union stands to gain greatly from Russia's accession to the WTO.”

¹⁸ See the “Speech by Peter Mandelson at the Joint Event Association of European Business (AEB) and the Russian Confederation of Business Industries (RSPP)”, Moscow, 27 March 2007, to be found

http://ec.europa.eu/commission_barroso/mandelson/speeches_articles/sppm144_en.htm
Mandelson, the EU Commissioner for Trade, said: “The WTO is not like the UN or the G8 - it's not simply about statehood or size. It is a contract based on commercial terms, creating legal obligations to openness and a commitment to transparent and proportionate regulation of trade. In trade terms, WTO exchanges the battlefield for the negotiating table, providing machinery for settling disputes without politicization and contamination of the wider inter-state relationship. Recent and current frictions in EU - Russia trade show the importance of de-escalating disputes.

Trade should never be treated as a political commodity by either side and should not give the impression of being used in such a way.” For a more straightforward but representative comment from the EU, see Inese Vaidere’s opinion (a Latvian MEP and a member of the Committee on Foreign Affairs): “In economic cooperation, Russia does not always keep to clear and fair rules of the game. Trade is often used as a foreign policy instrument. Very high demands are set upon the importers, and the compliance with these demands is tested during politically sensitive moments. Products that for many years have been very popular in Russia: Moldovan and Georgian wines, Georgian mineral water, Polish agricultural produce, Latvian and Estonian fishery products, have been subject to political manipulations, such as import embargos. Ukraine and Georgia have experienced sanctions through gas supplies.” In an article “EU must avoid hypocrisy with Russia”, 9 December 2006, to be found at http://www.neurope.eu/view_news.php?id=68116

¹⁹ To be found at http://www.eur.ru/en/p_245.htm

²⁰ Vladimir Putin, “50 Years of the European Integration and Russia”, 25 March 2007, to be found at

http://www.president.kremlin.ru/eng/speeches/2007/03/25/1133_type104017_120756.shtml While in the (official Kremlin) English version of Putin’s article this is actually expressed as “*Anything* but institutions”, the original Russian version with “vse, krome institutov” comes closer to the original. Putin apparently refers to Prodi’s well-known keynote speech:

“A Wider Europe - A Proximity Policy as the key to stability”, Speech by Romano Prodi, President of the European Commission, “Peace, Security And Stability International Dialogue and the Role of the EU” Sixth ECSA-World Conference. Jean Monnet Project, Brussels, 5-6 December 2002, SPEECH/02/619, to be found at

http://ec.europa.eu/comm/external_relations/news/prodi/sp02_619.htm In that speech Prodi stated: “On other occasions I have already referred to this concept, which I described as “sharing everything with the Union but institutions”. The aim is to extend to this neighbouring region a set of principles, values and standards which define the very essence of the European Union.”

²¹ See http://europa.eu.int/comm/external_relations/russia/summit_05_05/

²² It was the then Head of the European Commission Romano Prodi who proposed it to President Vladimir Putin. After a while, a High-Level Group, headed by the Commissioner Chris Patten and Deputy Prime Minister Viktor Khristenko, was established to elaborate the idea further.

²³ To be found as an English translation at the EU’s website

http://europa.eu.int/comm/external_relations/russia/summit11_03/1concl.pdf

²⁴ See Bela Balassa, *The Theory of Economic Integration*, London 1961.

²⁵ Table 1 source: The categories are based on the structure and prioritized issues identified in the Road Maps from 10th of May 2005, to be found from

http://ec.europa.eu/comm/external_relations/russia/summit_05_05/finalroadmaps.pdf#fsj

²⁶ Table 2 source: The categories are based on the structure and prioritized issues identified in *Road Map for the Common Economic Space – Building Blocks for Sustained Economic Growth* from 10th of May 2005, to be found at

http://ec.europa.eu/comm/external_relations/russia/summit_05_05/finalroadmaps.pdf#fsj

²⁷ To be found at http://europa.eu.int/comm/external_relations/ceeca/pca/pca_russia.pdf

²⁸ To be found at http://www.eur.ru/en/p_244.htm

²⁹ To be found at http://www.eur.ru/en/p_245.htm

³⁰ Should one compare these two documents (the 2003 *Concept Paper* and the 2005 *Road Map*), one can draw some conclusions. First of all, while the general aim in both is clearly towards a closer integration between the EU and Russia, the *Road Map* is, of course, more detailed and developed, especially adding some industrial products and fields – such as automotive industry, textile industry, medical devices etc. – explicitly into agenda as priority areas. Second, of the different instruments of the *Concept Paper*, the *Road Map* applies especially the idea of regulatory convergence and legal harmonization in many fields both as an instrument and as the final objective. Third, however, there are no time schedules or dead lines put

forward in the *Road Map*, which to some extent leaves the document largely as a political declaration of good purposes rather than a real action plan. Finally, some questions which are included in the earlier *Concept Paper* as goals, such as trade-related free(er) movement of persons, are not included in the *Road Map*.

³¹ In the preparation of the *Concept Paper*, however, the parties commissioned several economic impact studies, and at least one of them took the idea of an FTA literally, namely Paul Brenton, *The Economic Impact of EU-Russia Free Trade Agreement*, CEPS 2002, unpublished. However, this idea did not find its way into the official document.

³² (The EU's) *Country Strategy Paper 2007-2013, Russian Federation*, Section "3.4. Economic policy" (p. 10), to be found at http://ec.europa.eu/comm/external_relations/russia/csp/2007-2013_en.pdf

³³ For a comprehensive review, see Single Economic Space. Viability, implications and prospects. LSE & Eurasia Heritage 2005.

³⁴ As mentioned in the previous footnote, free movement of labour force or trade-related persons is a theme basically omitted in the *CES Road Map*, however. Nevertheless, the visa regime is dealt with in the Common Space of Freedom, Security and Justice.

³⁵ There are several analyses, which deal with the legal approximation between Russia and the EU. See, for instance: S. Kashkin, *Strategy and mechanisms of legislation harmonisation between Russia and the European Union as key components of their effective mutual development in the XXI century*, Moscow: RECEP 2005, to be found at http://www.recep.ru/files/documents/harmonization_kashkin_eng.pdf; D. Isaev, *Basic theories of harmonization of legislative in the process of forming of common spaces Russia-the EU* (in Russian only), Moscow: RECEP 2005, to be found at http://www.recep.ru/files/documents/harmonization_isaev_rus.pdf

³⁶ See Alfred E. Kellermann, *Membership of the European Internal Market without being an EU Member State*, Moscow: RECEP 2005.

³⁷ The basic philosophy of this approach could be questioned by asking why it is Russia and not the EU, or both, who should harmonise: Why could not the EU also harmonise its legislation according to Russian legislation? To this objection there are rather natural reasons for defending unilateral harmonisation by Russia – if the goal is integration. First, most or almost all of the legal harmonisation issues are of economic nature and the sheer difference of size of the economies of the EU and Russia suggests that the reverse process is unrealistic. Second, the EU is also overwhelmingly Russia's largest foreign trade partner with more than a fifty per cent share, while the EU's foreign trade with Russia plays only a minor role (although in energy the EU is largely dependent). Third, it is generally accepted that in most fields European legislation is better and more advanced as well as more suitable for forcing regional integrationist tendencies than Russian legislation, which is based on a protectionist philosophy in many fields.

³⁸ See http://ec.europa.eu/internal_market/ext-dimension/dialogues/index_en.htm

³⁹ Unless otherwise stated, the official documents and information mentioned in this section are taken from, and can be found from, the Ministry of Transport of the Russian Federation website <http://www.mintrans.ru> and especially from the ministry's strategies mentioned in the text and the following endnotes. Other general information is based on several years' study of the general debates and news on Russian transport sector, reflected especially in the following official (Ministry of Transport related) or unofficial (usually professional and interest organisations') websites and news sources: <http://www.asmap.ru>; <http://www.mbsz.ru/03/03.php>; <http://www.seanews.ru/>; <http://www.transport.ru/777/index.htm>; <http://www.transportrussia.ru>; <http://www.rg.ru/tema/ekonomika/transport/index.html>

⁴⁰ In fact, the current published authorised version (in Russian) is dated in 2005, and can be found at <http://mintrans.ru> under "Transportnaya strategiya". However, basically the same document can be found already in its 2004 version at http://www.mintrans.ru/pressa/Trans_Strat_08_12_2004.pdf

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- ⁴¹ Both documents to be found as packed files at <http://www.mintrans.ru/> (in Russian) under “Transportnaya strategiya”.
- ⁴² See <http://www.businesskomi.ru/11607/> (in Russian)
- ⁴³ This report has been extensively reviewed in Christer Pursiainen, *E 18 tien kehittämisselvitys 2002. Erillisselvitys Venäjän ja erityisesti Luoteis-Venäjän kehitysnäköymistä liikenteen näkökulmasta* [E 18 Road development conditions in North-West Russia], Tichallinto/LT-Consultants Ltd., Helsinki 21.10.2002. To be found at http://www.kolumbus.fi/christer.pursiainen/e18_luoteis_venajan_kehitys.pdf
- ⁴⁴ Source of Table 4: *Northwest Russia's federal district's social-economic strategy up to 2015* (2002 version, In Russian), reviewed in Christer Pursiainen, *E- 18 tien kehittämisselvitys 2002. Erillisselvitys Venäjän ja erityisesti Luoteis-Venäjän kehitysnäköymistä liikenteen näkökulmasta* [E 18 Road development conditions in North-West Russia], Tichallinto/LT-Consultants Ltd., Helsinki 21.10.2002. To be found at http://www.kolumbu.fi/christer.pursiainen/e18_luoteis_venajan_kehitys.pdf
- ⁴⁵ For a rather detailed statistics of the Northwest Russian road and other transport networks, see Christer Pursiainen 2002, *op. cit.*, to be found at http://www.kolumbus.fi/christer.pursiainen/e18_luoteis_venajan_kehitys.pdf From the European and especially the Northwest Russian perspective, one should notice that the federal roads are connected to the 9th trans-European corridor Helsinki-St. Petersburg-Moscow-Kiev-Kishinev, with a connection to the Kiev-Minsk-Vilnius-Kaliningrad and Pskov-Vitebsk-Kiev main roads. The federal roads are also connected to the European road network system through E-18 (“*Skandinaviya*”), E-20 (“*Narva*”), E-22 (“*Baltija*”), E-28 (Kaliningrad-Chernjahovsk-the state border of Lithuania), E-95 (St. Petersburg – the state border of Belarus) etc. The federal roads are most over-loaded, especially the “Rossiya” road (St. Petersburg-Moscow), where the traffic is 7000-12400 cars/day. In Northwest Russia the main road transport junction in Northwest Russia – both in relation to other Russian regions (Pskov, Novgorod and Moscow) as well as neighbouring countries – is St. Petersburg and the Leningrad region. Another important junction is the Vologda region with its link to Moscow. In Northwest Russian regions, especially the “*Skandinaviya*” road between the Finnish border station Vaalimaa and St. Petersburg, Kaliningrad-Chernjahovsk-Nesterov-the state border of Lithuania and St. Petersburg-Pskov main roads are heavily over-loaded.
- ⁴⁶ A Memorandum of Understanding on the creation of an EU-Russia Transport Dialogue was signed in October 2005. According to the EU information “The new dialogue should lead to stronger EU-Russia transportation and infrastructure links. It entails a regular exchange of information in order to create benefits for both economies and their consumers. [...] The Transport Dialogue will work on the basis of regular meetings on mutually agreed issues and topics within the framework of ad-hoc Working Groups. The following five Working Groups are currently foreseen: Transport strategies and Public-private partnership (PPP); Transport security; Air transport; Maritime, sea-river and inland waterway transport; and Road and rail transport.” See http://ec.europa.eu/comm/external_relations/russia/summit_10_05/ip05_1215.htm
- ⁴⁷ (The EU's) *Country Strategy Paper 2007-2013, Russian Federation*, Section “6.9. Thematic programmes”/”Transport” (p. 56), to be found at http://ec.europa.eu/comm/external_relations/russia/csp/2007-2013_en.pdf
- ⁴⁸ For European emission standards, see <http://www.answers.com/topic/emission-standard> or <http://www.transportenvironment.org/Article45.html>
- ⁴⁹ For the development of the private transport sector under market conditions in Russia in the 1990s, see V.I. Lyasko, *Strategicheskoe planirovanie razvitiya avtotransportnykh predpriyatij*, Moskva: Izdatel'stvo OOO Firma ‘Blagovest-B’ 2003, pp. 6-14.
- ⁵⁰ See <http://www.asmap.ru>
- ⁵¹ (The EU's) *Country Strategy Paper 2007-2013, Russian Federation*, Section “3.4. Economic policy”/”Transport” (p.12), to be found at http://ec.europa.eu/comm/external_relations/russia/csp/2007-2013_en.pdf
- ⁵² The description here is based on several years’ of research following the (mainly Finnish) newspaper reports of the “truck quarrel” between Finland and Russia; combined with

discussions with the Finnish transport authorities and interest organisation representatives, who deal with the issues in question; and access to the minutes of a number of meetings of the Finnish-Russian joint committees at different levels on transport.

⁵³ *Tapaustutkimus kuljetuksista Suomen ja Venäjän rajan yli (FIRUCASE)*, TEDIM julkaisut 2005.

⁵⁴ Unless otherwise stated, the official documents and information mentioned in this section are taken from and can be found at the Ministry of Transport of the Russian Federation website <http://www.mintrans.ru>. Other general information is based on several years' study of the general debates and news on Russian transport sector, reflected especially at the following official (Ministry of Transport related) or unofficial (usually professional and interest organisations') websites and news sources: <http://www.mbsz.ru/03/03.php>; <http://www.seanews.ru/>; <http://www.transport.ru/777/index.htm>; <http://www.transportrussia.ru/>; <http://www.rg.ru/tema/ekonomika/transport/index.html> A good survey of especially Northwest Russian port sector from statistical perspective can also be found in Christer Pursiainen 2002, *op. cit.*, to be found at http://www.kolumbus.fi/christer.pursiainen/e18_luoteis_venajan_kehitys.pdf

⁵⁵ Both above mentioned documents can be found as packed files at <http://www.mintrans.ru/> (in Russian) under "Transportnaya strategiya".

⁵⁶ The current published authorised version (in Russian), dated in 2005, can be found at <http://mintrans.ru> under "Transportnaya strategiya". However, basically the same document can be found already in its 2004 version at http://www.mintrans.ru/pressa/Trans_Strat_08_12_2004.pdf

⁵⁷ For instance: "The centre of Russian economic gravity lies clearly in the west. Russia has come to know the "Rotterdam syndrome", being dependent on ports outside her sovereign control. The Baltic ports, non-Russian and Russian alike, are essential gateways for exports and imports. Attempts to resist interdependence, this most European of phenomena, echo Soviet autarky thinking." René Nyberg, Ambassador Head of Division for Eastern Affairs Ministry for Foreign Affairs of Finland St Antony's College Oxford, 8 May 2000, "The Baltic as an Interface Between the EU and Russia", to be found at <http://formin.finland.fi/Public/Print.aspx?contentid=51283&nodeid=15553&culture=en-US&contentlan=2>; see also Ambassador René Nyberg, "The Baltic - a future inland sea of the European Union", Ripon Educational Fund's 1999 TransAtlantic Conference 19 August 1999, Stockholm, to be found at <http://presidency.finland.fi/netcomm/News/showarticle770.html> Nyberg said: "The Russia of today is more dependent on foreign trade than the Soviet Union ever was. Almost half of its seaborne trade crosses the Baltic. This interdependence is aptly called the Rotterdam syndrome. Germany's largest port is Rotterdam in the Netherlands, not Hamburg. -- You don't have to own or control a port in order to use it."

⁵⁸ These figures come from the Northwestern federal district's transport strategy, reviewed in Christer Pursiainen 2002, *op. cit.*, to be found at http://www.kolumbu.fi/christer.pursiainen/e18_luoteis_venajan_kehitys.pdf

⁵⁹ For detailed and reasonably updated information about the main ports in Northwest Russia, see their own or closely related websites (the following websites can be found, usually in both Russian and English): St. Petersburg port <http://www.seaport.spb.ru/>; Vyborg port <http://www.port.vyborg.ru/eng/index.html>; Vysotsk port <http://www.vyborg.ru/org/baff/66.htm>; Ust-Luga port <http://www.ust-luga.ru/>; Kaliningrad port <http://portfocus.com/russia/kaliningrad/index.html>; Murmansk port <http://www.russia.com/ports/murmansk/>; Arkhangelsk port <http://www.arhport.ru/> There are also several rather detailed analyses on the theme from a various perspectives (the problem of these analyses is, however, that they tend to become partially outdated very quickly because of the dynamics of the sector). To mention but some: Alf Brodin, *The Russian Port Sector in the Baltic Sea Region*, Centrum för Europaforskning CERGU, Göteborgs University, CERGU's Project Report Series No 00:2, May 2000. For a more comprehensive work including the same information, see Alf Brodin's PhD dissertation: *Baltic Sea Ports and Russian Foreign Trade - Studies in the Economic and Political Geography of Transition*, Handelshögskolan vid Göteborgs Universitet, Meedelanden från Göteborgs

universitetets geografiska institutioner serie B, NR 104, March 2003. Also to be found in electronic version at <http://www.handels.gu.se/epc/archive/00002983/01/BrodinAvh.pdf> Rather detailed information on the ports from the perspective of maritime oil transportation can be found from Kari Liuhto (edited on the basis of the analyses of Elena G. Efimova, Liudmila V. Popova, Sergei F. Sutyryn), *Growing Russian oil shipments in the Baltic Sea: Strategic decision or environmental risk?* Lappeenranta University of Technology 2003, to be found at <http://www.worldec.ru/content/lecturers/articles/article-05.pdf>

⁶⁰ Brodin 2000, op. cit., p. 36.

⁶¹ Often also the project documentation is fraudulent from an environmental impact point of view. To illustrate this, when the oil company *Lukoil* began the construction of the Vysotsk oil terminal in 2002, it proceeded with the work based on a different project for that which it had a license. When this was revealed, there were no serious consequences, however, and after preparing the formally necessary new documents the project continued as before.

⁶² Sometimes there are also disagreements between the regions and the federation in respect of the practical implementation of the projects, especially when it comes to federal financing. To illustrate a typical quarrel, in 2002 the federal government approved the project aiming at the construction of the infrastructure arrangements for transport from the Ust-Luga port in the Leningrad region to the Baltic Sea port of the Kaliningrad region and further on to German ports. The federation promised funding for the port infrastructure, which belongs to state responsibilities in accordance with the legislation, and it also promised to provide state guarantees for bank loans. One of the prospective lenders was the European Bank of Reconstruction and Development (EBRD). The governor of Leningrad region did not however agree to begin the project and accept the EBRD loan before the federation had concretely put the promised budgetary funding in place.

⁶³ An English-language summary can be found at http://ec.europa.eu/energy/russia/events/doc/2003_strategy_2020_en.pdf

⁶⁴ There are, however, considerable differences between the “optimistic” and “pessimistic” scenarios of Russia’s oil production capacity (see, for instance the <http://www.iea.org/textbase/papers/2003/strategy2020.pdf>). The bottleneck is the need for extensive investments for both the modernization of old oil fields and the utilization of new fields as well as the transport routes and infrastructure. As to oil resources, the estimations differ between 60-75 Billion barrels (see <http://www.eia.doe.gov/emeu/international/reserves.html>), which means that after the Middle East oil producing giants and Venezuela, Russia will nevertheless remain a major actor in the field. For Northwest Russian perspective in particular, see also: Kari Liuhto (2002b), *Russian oil and gas – A source of integration*, Research report N:o 131 2002, Lappeenranta University of Technology; Liuhto (ed. 2003), *op. cit.*

⁶⁵ For a detailed case studies of the mechanisms of how the civil society works in Russia in trying to influence the authorities, see Oleg N. Yanitsky, *Russian Greens in a Risk Society*, Kikimora publications, Helsinki 2000.

⁶⁶ *The Russian Environmental Digest*, 9 - 15 October 2000, Vol. 2, No. 41, and the subsequent issues of the same electronic journal.

⁶⁷ Tens or hundreds of environmental NGOs are active in Northwest Russia. Only in St. Petersburg, there are about 160 environmental NGOs, see *A Directory of Non-Government Environmental Organizations of St. Petersburg*, Transboundary Environmental Information Agency: Notabene Publishers 1998. Some of the perhaps most well-known (purely Russian or transnational Russia-based) environmental organizations, active in Northwest Russia, include *Ecodefence* <http://www.ecodefence.ru>; *Green World* <http://www.greenworld.org.ru/>; *The Socio-Ecological Union* <http://www.seu.ru/seu-news/eng/soccco11.htm>; *Russian Greenpeace* <http://www.greenpeace.org/russia/en/>; the Russian branch of the Norwegian *Bellona* <http://www.bellona.org/>. A good source of general information is the St. Petersburg –based

Transboundary Environmental Information Agency (TEIA) <http://teia.ru/> who publishes the electronic, free and English-language *Russian Environmental Digest*.

⁶⁸ See Christer Pursiainen, “The Development of Civil Society – State Relations in Russia”, in *Good Governance and the Administrative Reform. Towards a New Contract of the State, Business and Civil Society in Russia*, edited by S. Medvedev, Moscow: RECEP 2007.

⁶⁹ The head of FSB in St. Petersburg and Leningrad region, Sergei Smirnov, as reported in V. Toropchin’s article ‘Glavnaya ugroza – terrorizm’, *Novosti Leningradskoy Oblasti*, April 2001.

⁷⁰ *Russian Environmental Digest*, 25 - 31 July 2005, Vol. 7, No. 31 (item 8).

⁷¹ Ibid.

⁷² *The Russian Environmental Digest* 2 - 8 October 2000, Vol. 2, No. 40, article 2, and ibid 9 - 15 October 2000, Vol. 2, No. 41, articles 3 and 4.

⁷³ *Green World Baltic News* 56, 27 Nov., 2000 (item 1).

⁷⁴ *Russian Environmental Digest*, 8 - 14 May 2006, Vol. 8, No. 20 (item 2).

⁷⁵ Unless otherwise stated, the official documents and information mentioned in this section are taken from and can be found at the website of the Ministry of Natural Resources of the Russian Federation <http://www.mnr.gov.ru/part/?pid=800> and its subordinated agency, the Federal Agency of Forestry <http://les.mnr.gov.ru/>. There are several good and statistically sophisticated surveys of Russia’s forestry sector: A good review of qualitative-quantitative information is the power point presentation of Director of the Federal Agency of Forestry Management of the RF, R.V. Roshchupkin: “On the fulfilment of the measures for the realization of the concept of the development of forestry in the Russian Federation 2003-2010”, November 2005, to be found at http://www.mnr.gov.ru/files/part/7348_prezent.ppt. Another good analysis is *Risks and rewards. Forest, paper & packaging in Russia*, PrivateHouseCoopers, October 2006, to be found at [http://www.pwc.com/Extweb/pwcpublishings.nsf/docid/C0F928879D4E4C6C85257206007CD790/\\$File/risks-rewards_fpp-in-russia.pdf](http://www.pwc.com/Extweb/pwcpublishings.nsf/docid/C0F928879D4E4C6C85257206007CD790/$File/risks-rewards_fpp-in-russia.pdf). See also: Antti Mutanen, Jari Viitanen, Anne Toppinen, Riitta Hänninen & Päivi Holopainen, *Forest resources, production and exports of roundwood and sawnwood from Russia*, Finnish Forest Research Institute, Joensuu Research centre 2005, can be found at

<http://www.metla.fi/julkaisut/workingpapers/2005/mwp009.htm>. Other general information is based on continuous monitoring of the following websites and news sources: the Internet version of “Russian Forest Newspaper” <http://hosting.rbc.ru/ru/>; a major Russian forest sector specialized website <http://www.lesprom.ru/>; Russian NGO site including forest related material and a very useful further link list <http://www.forest.ru/>; Food and Agriculture Organization of the United Nations, including Russia-specified descriptions and statistics <http://www.fao.org/forestry/index.jsp>; World Forestry Center, USA-based NGO site, including Russia-specified descriptions and statistics <http://wfi.worldforestrycenter.org>; Global Forest Watch NGO’s informative website with material on Russia’s forests <http://www.globalforestwatch.org/english/russia/news.htm>; a collection of practical information and news on Russia’s forest sector in Finnish and Russian <http://www.idanmetsatieto.info/fi/cfmldocs/>.

⁷⁶ The figures put forward in Russian analyses show that while in Finland, Sweden, USA and Norway there are 40, 11, 10 and 9 km/ha of forest roads respectively, in Russian forests the figure is only 1.2 km/ha. Furthermore, the problem here is not only the absence of forest roads but the bad condition of the existing ones. In any case, the average transport length for available timber from the forests to the production sites has quadrupled over the past fifteen years. This line of argument is a standard element in almost all speeches and articles of the Director of the Federal Agency of Forestry Management of the RF, R.V. Roshchupkin, see for instance, his article in *Rossiyskaya gazeta* 16 February 2006, to be found at <http://les.mnr.gov.ru/part/?act=more&id=1130&pid=253>. However, from company point of view this seems to be not so big a problem. In a 2007 study, based on interviews of managers of some major Northwest Russian woodworking companies, the interviewed emphasised “closeness to the markets, good logistic connections and large market size” as the main sources of the

companies' competitive advantage. "Forest resources and availability of wood raw material or price of wood raw material were not considered as particularly significant sources of competitive advantage. The overall reliability, good image and reputation of the company and its qualified and skilled personnel were the most important factors in which the interviewed managers of case companies estimated to be in the best competitive position against their rivals. High taxation, corruption and lack of capital strongly characterised the problems present in their business environment." See A. Toppinen, R. Toivonen, E. Järvinen, V. Goltsev, N. Tatti & A. Mutanen, *Business environment and strategies of wood industry companies in Leningrad and Vologda regions – results from a pilot study*, Working Papers of the Finnish Forest Research Institute 41, to be found at <http://www.metla.fi/julkaisut/workingpapers/2007/mwp041.htm>

⁷⁷ Presentation of Director of the Federal Agency of Forestry Management of the RF, R.V. Roshchupkin: "On the fulfilment of the measures for the realization of the concept of the development of forestry in the Russian Federation 2003-2010", November 2005. To be found at http://www.mnr.gov.ru/files/part/7348_prezent.ppt

⁷⁸ This was one of the main concerns discussed during President Putin's visit to Syktyvkar, Komi Republic, with all the ministers concerned, organized for discussing the state of Russia's forestry sector; see *Lesnaya Gazeta* 6 April 2006.

⁷⁹ To be found at <http://les.mnr.gov.ru/part/?pid=243>

⁸⁰ To be found at <http://les.mnr.gov.ru/part/?pid=243>

⁸¹ This and the forthcoming sections are largely based on information and briefings received from the forestry specialist at the Finnish Embassy in Moscow, Counsellor Hannu Kivelä, with some updating from recent news sources and the internet sources referred to above. All misunderstandings and mistakes are naturally the author's responsibility.

⁸² Russia is raising its round wood export duties at a fast pace: 1 June 2007 20% min 10 euro/m³ for fir, pine tree as well as birch over 15 cm and 10% min 5 euro/m³ for aspen; 1 April .2008 25% min 15 euro/m³ for fir, pine tree as well as birch over 15 cm) and 10% min 5 euro/ m³ for aspen; 1 January 2009 80% min 50 euro/m³ for fir, pine tree, aspen as well as birch over 15 cm; 1 January 2011 80% min 50 euro/m³ for fir, pine tree, aspen as well as birch. Source: Presentation of Councillor Hannu Kivelä, Finnish Embassy to RF, "Venäjän puuntuonnin tulevaisuus", at *Metsäpäivät 2007* in Helsinki 20 March 2007, to be found (in Finnish) at [http://www.metsapaivat.fi/smy/Materiaalitdeve.nsf/allbyid-MP/3298F5D54072E98CC22572A40035897A/\\$file/Metsapaivat2007-HannuKivela.pdf](http://www.metsapaivat.fi/smy/Materiaalitdeve.nsf/allbyid-MP/3298F5D54072E98CC22572A40035897A/$file/Metsapaivat2007-HannuKivela.pdf)

⁸³ See, for instance: "EU and Russia still at odds over wood export duties" (28 March 2007) to be found at <http://www.hs.fi/english/article/EU+and+Russia+still+at+odds+over+wood+export+duti+es/1135226175269>; or "Russian export tariff could end timber imports into Finland. [Minister] Lehtomäki accuses Russia of violating WTO treaty" (12 February 2007) to be found at

<http://www.hs.fi/english/article/Russian+export+tariff+could+end+timber+imports+into+Finland/1135225040316>; or "Increase in price of Russian wood forcing changes on Estonian sawmills" (13 February 2007 *Baltic Service News*) to be found at <http://ee2.mofcom.gov.cn/aarticle/chinanews/200702/20070204382939.html>

⁸⁴ See, for instance, the comments of the representatives of Finnish forestry industry in the article "Russian export tariff could end timber imports into Finland. [Minister] Lehtomäki accuses Russia of violating WTO treaty (12 February 2007) to be found at <http://www.hs.fi/english/article/Russian+export+tariff+could+end+timber+imports+into+Fi+mland/1135225040316>

⁸⁵ This section is largely based on information and briefings received from the forestry specialist at the Finnish Embassy in Moscow, Counsellor Hannu Kivelä, with some updating from recent news sources and the internet sources referred to above. All misunderstandings and mistakes are naturally the author's responsibility.

⁸⁶ This section is partially based on a good survey of the development of Russia's timber industry, written by Dmitry Butrin for the newspaper *Kommersant*, to be found at

http://www.kommersant.com/tree.asp?rubric=3&node=43&doc_id=487624; as well as http://www.kommersant.com/t487624/r_3/n_43/Timber_Industry_2000-2004/

⁸⁷ “While most of the equipments, machinery and capacity investments in Russian forest sector dates back to 1970’s, they are mostly out-of-date, wastefully, environmentally damaging and the productivity of them is weak. Domestic possibilities to finance forest investments in Russia are still under developing, and the forest sector is not attractive among Russian investors due to the more profitable sectors such as energy, technology and metal clusters. Therefore, the forest sector calls urgently for forest investments to develop, to create more value added production and to survive in international competition in final product markets.” Quotation from Päivi Holopainen, Pekka Ollonqvist, & Jari Viitanen, *Factors affecting investments in Northwest Russian forest sector and industry*, Working Papers of the Finnish Forest Research Institute 32, to be found

at <http://www.metla.fi/julkaisut/workingpapers/2006/mwp032.htm>

⁸⁸ For instance, the Finnish Metsäliitto Group, the tenth largest forest industry group in the world, writes on its website as follows: “About 95% of this [Russian] wood is delivered to Metsäliitto Group's mills in Finland, with most of the remainder going to Sweden, a small amount to Norway, and some to external customers. Metsä-Botnia’s sawmill OOO Svir Timber in Podporozhye, which was inaugurated on 7 June 2006, is also a significant customer for Wood Supply Russia.” See <http://www.metsaliitto.com/page.asp?path=1:2785:2804:2911>; for Finnish forestry industry, import from Russia makes approximately 22% of all wood used in factories and for some factories this figure is as high as 80% Presentation of Councillor Hannu Kivelä, Finnish Embassy to RF, “Venäjän puuntuonnin tulevaisuus”, at *Metsäpäivät 2007* in Helsinki 20 March 2007, to be found (in Finnish) at

[http://www.metsapaivat.fi/smy/Materiaalitdeve.nsf/allbyid-MP/3298F5D54072E98CC22572A40035897A/\\$file/Metsapaivat2007-HannuKivela.pdf](http://www.metsapaivat.fi/smy/Materiaalitdeve.nsf/allbyid-MP/3298F5D54072E98CC22572A40035897A/$file/Metsapaivat2007-HannuKivela.pdf)

⁸⁹ See, for instance the descriptions of the Finnish StoraEnso’s Russian mills at http://www.storaenso.com/CDAvgn/main/0,1_EN-6518-14324,00.html

⁹⁰ According to Director of the Federal Agency of Forestry Management of the RF, R.V. Roshchupkin. A summary of his presentations, dated 24 March 2006, is to be found at the website of the Ministry of Natural Resources at <http://www.mnr.gov.ru/part/?act=more&id=1820&pid=11> , dated 24 March 2007. In this occasion Roshchupkin noticed that illegal logging in Europe does not exceed 3%, in the USA and Canada 1%, in Japan 3-5%, while in Brazil it comprises more than 20%. According to Russian Natural Resources Ministry statement in 2005, the damage from illegal logging in Russia comes up to 5 billion rubles (some 180 million USD) annually. It was stated that “Together with Brazil, Cameroon, Gabon, Indonesia and Malaysia, Russia is among the leaders in illegal tree felling”. According to the ministry, illegal logging accounts for 89% of violations of the Russian forest legislation, with only 10% of cases of illegal use of the forest resources reaching the court. Source: *Russian Environmental Digest*, 30 May - 5 June 2005, Vol. 7, No. 23 (item 8).

⁹¹ See, for instance, “Illegally cut timber among Russian imports to Finland. Russia hopes to weed out illegal felling”, in the electronic international edition of *Helsingin Sanomat* 27 October 2004, to be found at

<http://www.hs.fi/english/article/Illegally+cut+timber+among+Russian+imports+to+Finland/1076154357645>

⁹² In 2006, the satellite control observed about 1 Million m³ illegal logging. This monitoring covered 18 regions (of 89) or altogether 101,2 Million ha. Most illegal logging took place in Krasnoyarsk, Irkutsk, Arkhangel Tomsk and Chita. Source : A news, dated 17 April 2007, “Laittomien hakkuiden satelliittivalvonnan tulos vuonna 2006” (in Finnish), to be found at http://www.idanmetsatieto.info/fi/cfmldocs/index.cfm?ID=270&tiedote=view&tiedote_ID=1274

⁹³ (The EU's) *Country Strategy Paper 2007-2013, Russian Federation*, Section "1. Executive Summary", to be found at http://ec.europa.eu/comm/external_relations/russia/csp/2007-2013_en.pdf

⁹⁴ The following nine Sub-Committees exist according to the PCA: 1) Trade and industry; 2) Energy, environment and nuclear issues; 3) Science and technology, human resources, social co-operation; 4) Transport, telecommunications and space; 5) Coal and steel, mining and raw materials; 6) Competition, IPR, approximation of legislation, fight against crime; 7) Customs and cross-border co-operation; 8) Agriculture, fisheries, consumer protection; 9) Financial and economic issues, statistics.