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# **DEALING WITH A POST-BRIC RUSSIA**

**Ben Judah, Jana Kobzova  
and Nicu Popescu**

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© ECFR November 2011.

ISBN: 978-1-906538-40-8

Published by the European Council on Foreign Relations (ECFR), 35 Old Queen Street, London, SW1H 9JA, United Kingdom

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# Acknowledgements

The report has benefitted from extensive field research. The authors travelled to Russia in December 2010 and for a month of research in May 2011. In the neighbourhood the authors conducted research in Moldova, Ukraine, Georgia and Armenia. A two-week study trip was also conducted in Beijing and Shanghai in June 2011. Within the European Union interviews were conducted in Austria, Belgium, Bulgaria, Czech Republic, Denmark, France, Germany, Italy, Poland, Romania, Slovakia, Slovenia and the United Kingdom. We would like to thank numerous colleagues, diplomats, experts and politicians who have given us time, advice or practical assistance whilst working on this report:

Matti Anttonen, Ilya Arkhipov, David Bartels, Nicolaas Bel, Sergei Belokonev, Oskar Benedikt, Chris Bobinski, William Boe, Joerg Bongartz, Timofei Bordachev, Ulrich Brandenburg, Laurie Bristow, James Brooke, Laurence Broyd, William Browder, Manuel de la Camara, Jin Canrong, Andrzej Cieszkowski, Santiago Chamorro, Konstanin Chernyshev, Alexey Devyatov, Peter B. Doran, Remi Dufлот, Konstantin von Eggert, Fatma Ceren Yazgan Etiz, Raphael Fisera, Joerg Forbrig, Hovhannes Ghazaryan, Viacheslav Glazychev, Alexander Golts, Petra Gombalova Kyslingerova, Karoly Gruber, Lev Gudkov, Sergei Guriev, Guan Guihai, Zhang Haiyang, Jacqueline Hale, Tony Halpin, Hiski Haukkala, Karel Hirman, Cui Hongjian, Vladislav Inozemtsev, Christoph Israng, Igor Ivanov, Kestutis Jankauskas, Balazs Jarabik, Vuk Jeremic, Ni Jianjun, Tim Judah, Liu Jun, Oleg Kashin, Andrey Kazantsev, Denis Keefe, Matus Korba, Martin Kosatka, Tomas Kozak, Gerald Knaus, Andrzej Kneifel, Simon Kordonsky, Katarina Kralikova, Andrew Kramer, Mikhail Krutikhin, Miroslav Lajcak, Yulia Latynina, Iurie Leanca, Masha Lipman, Yaroslav Lissovolic, Bobo Lo, Edward Lucas, Alexander Lukin, Fyodor Lukyanov, Mikhail Lysenko, Denis MacShane, Madeleine Majorenko, Jan Marian, Sergei Markov, Dzianis Meliantsov, Marie Mendras, Fu Mengzi, Stefan Meister, Boris Mezhuyev, James Miles, Artur Michalski, Vladimir Milov, Wess Mitchell, Alexander Morozov, Alexey Navalny,

Alena Obrusnikova, Cornelius Ochmann, Bogumila Ordyk, Arkady Ostrovsky, Gleb Pavlovsky, Ding Peihua, Roberto Pelo, Vadim Pistrinciu, Alexander Pivovarsky, Alexander Plekhanov, Tevan Poghosyan, Ruslan Pukhov, Chen Qingyi, William Rice, Norbert Riedel, Dmitry Rogozin, Katarzyna Rybka-Iwanska, Vladimir Ryzhkov, Mark Sabah, Pavel Salin, Alexander Savelyev, Dora Schaffrin, Igor Shchegolev, Hans-Jochen Schmidt, Susanne Schuetz, Hans-Henning Schroeder, Peter Semneby, Feng Shao Lei, Jeremy Shapiro, Lilia Shibanova, Olga Shumylo-Tapiola, Martin Sieg, Vitali Silitski, Eugeniusz Smolar, Vladimir Socor, Andrei Soldatov, Vladimir Solovyev, Franklin Steves, Susan Stewart, Dmitry Suslov, Sandor Szelekovszky, Pirkka Tapiola, Vessela Tcherneva, Elisabeth Teague, Rosemary Thomas, Ansgar Tietmeyer, Dmitri Trenin, Viorel Ursu, Sergey Utkin, Irina Varskaya, Dmitry Vasiliev, Alexander Voskresensky, Chris Weafer, Michael Webb, Fredrik Wesslau, Nicholas Whyte, Peter Whyte, Jakub Wisniewski, Marcin Wojciechowski, Yury Yarotsky, Shi Yinhong, Jiang Yong, Igor Zadorin, Wojciech Zajackowski, Ji Zhiye, Li Ziguo, Oleg Zykov and Anton Zykov.

Special thanks go to Matthew Rojansky and Tomas Valasek for their insights on US foreign policy and to Elena Gnedina, Martin Kaco, Rastislav Mojto and Stanislav Secrieru for both sharing their expertise and reading earlier drafts of this report.

We have also relied significantly on the expertise and assistance of our colleagues in European embassies abroad, many of whom have requested to remain anonymous. In Moscow we would like to thank the embassies or delegations of the Czech Republic, Denmark, Estonia, the European Union, Finland, France, Germany, Israel, Italy, Lithuania, the Netherlands, Poland, Slovakia, Spain, Sweden, Turkey, the United Kingdom, the United States, and Ukraine, as well as the Association of European Business. In Beijing we would like to thank the European Chamber of Commerce and the embassies and delegations of Denmark, the European Union, France, Germany, Georgia, Moldova, the Netherlands, Poland, the United Kingdom and the United States. In London we would like to thank some of the colleagues working at the embassies of Latvia, Lithuania, Mexico, Moldova, Poland, Slovakia and Ukraine.

We would like to thank members of the ECFR Council who have helped us to shape some of our arguments or commented on this report: Martti Ahtisaari, Emma Bonino, Heather Grabbe, Karin Forseke, Jaakko Iloniemi, Minna Jarvenpaa, Ivan Krastev, Nils Muiznieks, Giuseppe Scognamiglio, Radoslaw Sikorski, Aleksander Smolar, Javier Solana, Ion Sturza, and Vaira Vike-Freiberga.

At ECFR we are indebted to our research assistants Ben Shaps and Maria Sizyakova for all their hard work. We'd also like to thank our colleagues Dimitar Bechev, Olaf Boehnke, Nikoleta Gabrovska, Konstanty Gebert, François Godement, Daniel Korski, Alba Lamberti, Mark Leonard, Marta Makowska, Felix Mengel, Jonas Parello-Plesner, Alice Richard, Nicholas Walton, Andrew Wilson and, above all, the editorial expertise of Hans Kundnani whose guidance has sharpened not only our prose but also our arguments.

Although we have been informed by the discussions with those listed and many others, responsibility for the arguments and analysis advanced in this paper lies with the authors alone.





# Executive Summary

The global economic crisis has shattered Russia's dream of being a BRIC that is on a par with China, India and Brazil. Back in 2007, when the European Council on Foreign Relations published its *Power Audit of EU-Russia Relations*, Russia believed it was a rising power. As president from 2000 to 2008, Vladimir Putin was the incarnation of this vision of a resurgent Russia. During his time as president, he pursued a "divide and rule" policy towards the European Union and thus frustrated the EU's foreign-policy ambitions. But Russia no longer has the optimism of a rising power. Instead, it has the pessimism of the West.

The EU has spent the last four years wishfully thinking that Putin's successor as president, Dmitry Medvedev, would slowly transform Russia into a modern country and therefore a better partner. Now Putin is returning to the presidency and frontline foreign policy. Some fear this will mean a return to the foreign policy of his first two terms as president. But Putin has returned to a different Russia. Few still have any illusions about resurgence and many now fear stagnation and "Brezhnevisation". In other words, regardless of Putin's return and his assertive rhetoric, Russia is now "post-BRIC". The economic crisis has laid bare Russia's governance crisis. Growth is also being constrained as a consequence of weak institutions, the personalisation of power and fusion of property and power that defines Russian politics.

These changes have also forced Moscow to pursue a more cautious foreign policy. In particular, diminished economic expectations and the increased presence of other actors in the region have seen Moscow craft a new strategy for the post-Soviet space. Though it has not given up its hegemonic ambitions, expressed in Putin's proposal for a Eurasian Union, Russia now aims for a lower-cost sphere of influence. It is deploying limited resources selectively to create a kind of "lily-pad empire" – a network of military bases, pipelines and strategic chunks of national economies that clearly clashes with the EU's own neighbourhood policy.

Prior to the crisis, Russia hoped that, together with China, it could form a counter-hegemonic bloc that would dilute US unipolarity. But China is no longer an emerging market but an emerging superpower that increasingly sees Russia as a junior partner. Economic relations between the two countries are still growing, but they are increasingly imbalanced. Many in China have come to share the EU's frustration at the poor Russian business climate and rampant corruption, Russia's energy partnership with China is less promising than it once appeared to be, and the Russia-China security relationship is eroding.

Since 2008, there has also been a "reset" in the relationship between the United States and Russia. As the US shifts its attention away from the Atlantic and towards the Pacific, Russia has become a lower priority. There has been much discussion of the new US strategy of "leading from behind". However, in Russia, Eastern Europe and the North Caucasus, it is "leaving from behind". This change has created the basis for improvement for a more "transactional" relationship with Russia. The EU has benefited from the "reset". But it has yet to come up with a coherent strategy of compensating for, or adapting to, the US's relative de-prioritisation of Russia, Eastern Europe and the South Caucasus.

During the last few years, there have been two important developments that could give the EU greater leverage over Russia than in the past. The first is that the EU has taken steps to reduce its energy vulnerability towards Russia. Since 2009, the EU has accelerated attempts to revamp energy infrastructure to help avoid or better deal with potential cut-offs. The second is that member states have become less divided in their views of, and approaches to, Russia. Since 2008, member states have moved from the two extremes of engagement and containment towards the centre ground. In particular, Germany, arguably Russia's best friend in the EU, has become more hard-nosed, and Poland has "normalised" its on-tense relationship with Moscow.

However, despite greater unity, the EU has almost completely given up foreign policy ambitions on Russia. It now seems reconciled to accepting Russia as a "small China" with which it does business but does not criticise or try to change. The EU-Russia Partnership for Modernisation – the EU's flagship project – has been undermined by the separate bilateral partnerships that 18 of the EU's 27 member states have with Russia. Moreover, EU member states' visa policies are so divergent that the EU does not get the "soft power" benefits of being seen as a welcoming destination for Russian travelers but is also unable to use the prospect of visa-free travel to gain significant political concessions from Russia.

As the prospect of a two-speed Europe on economic issues emerges, foreign policy is unlikely to escape unscathed. However, the EU cannot afford the luxury of not having a Russia policy. Russia could either be a security problem for Europe or a strong partner that could strengthen Europe's stability and economic dynamism. Either way, the EU needs a strategy for a post-BRIC Russia. Such a strategy should be centered around further strengthening its unity and deepening engagement with Russia while creating disincentives for Russian officials to violate human rights and constraining Russia's claims to a "lily-pad" empire in the post-Soviet space. In short, the EU should engage Russia, but limit Putin's room for manoeuvre.

To strengthen unity, EU member states should:

- co-ordinate bilateral Partnerships for Modernisation and help Russia to meet OECD entry requirements.
- pass a European anti-corruption law based on the UK's recent Bribery Act 2010.
- launch an EU Business-to-Diplomats Taskforce.
- support EU companies to renegotiate gas-price formulas with Gazprom.

A stronger EU could then proactively re-engage Russia by:

- adopting an electronic visa system with Russia that drastically facilitates travel in the short term and is followed by a visa-free regime once Russia meets the necessary conditions.
- creating an EU-US-Russia partnership in Central Asia.
- developing co-operation with the CSTO and the Shanghai Cooperation Organisation.
- striking a grand bargain on EU-Ukraine free trade

In order to constrain Putin, the EU should:

- adopt a visa ban and asset freeze for those involved in the death of Sergei Magnitsky.
- support implementation of the energy *acquis* in the neighbourhood.
- expand security co-operation with the EU's eastern neighbours.
- make Russia an issue in EU-China relations.



## *Introduction*

# Putin's return to a post-BRIC Russia

The global economic crisis has shattered Russia's dream of being a BRIC that is on a par with China, India and Brazil.<sup>1</sup> Back in 2007 Moscow was a city with the political swagger and foreign-policy debate of a rising power: fired by high-growth rates and rising oil prices, Russia believed it was fireproof.<sup>2</sup> As president from 2000 to 2008, Vladimir Putin was the incarnation of this vision of a resurgent Russia. During his time as president, he pursued a "divide and rule" policy towards the European Union and thus frustrated the EU's foreign-policy ambitions. But some of the pro-Kremlin thinkers who were convinced that Russia was rising with the other BRICs now fear it is declining with the EU. Russia no longer has the optimism of a rising power. Instead, it has the pessimism of the West.

The EU has spent the last four years wishfully thinking that Putin's successor as president, Dmitry Medvedev, would slowly transform Russia into a modern country and therefore a better partner. Now Putin is returning to the presidency and thus to frontline foreign policy. Some fear this will mean a return to the foreign policy of his first two terms as president. But within Russia many now fear stagnation and "Brezhnevisation" instead. In other words, regardless of Putin's return and his assertive rhetoric, Russia is now "post-BRIC". Although it is not in steep decline, it is stagnating, with widespread corruption, a dysfunctional government and growing dissatisfaction with the ruling elite. Without drastic – but unlikely – improvements in the way it is governed, it clearly cannot keep pace with the dynamism and the growth perspective of the other BRICs.

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<sup>1</sup> The term "BRIC" was first used in a Goldman Sachs briefing paper in 2003. See Dominic Wilson and Roopa Purushothaman, "Dreaming With BRICs: The Path to 2050", Goldman Sachs Global Economics Paper No: 99, October 2003, available at <http://www.worldbpoforum.com/files/casestudy/2case.pdf> (hereafter, Wilson and Purushothaman, "Dreaming With BRICs").

<sup>2</sup> Mark Leonard and Nicu Popescu, "A Power Audit of EU-Russia Relations", European Council on Foreign Relations, November 2007, available at [http://www.ecfr.eu/content/entry/commentary\\_pr\\_russia\\_power\\_audit/](http://www.ecfr.eu/content/entry/commentary_pr_russia_power_audit/) (hereafter, Leonard and Popescu, "A Power Audit of EU-Russia Relations").

As the EU struggles to deal with the euro crisis and faces the possibility of what Christine Lagarde has called a “lost decade”, it must also find a way to engage with a post-BRIC Russia. The United States is gradually deprioritising Russia and Eastern Europe as it refocuses on the Pacific. The EU, which does not have the luxury of doing the same, will therefore have to play much of the political role traditionally taken by the US in the region. As a partner, Russia could help strengthen European stability and economic dynamism on the continent. As a threat, on the other hand, it would constitute a constant challenge to EU unity and its regional interests. But whether the EU wants to exploit the possibility of a partnership with Russia or minimise the threat from Russia, it needs a strategy for a post-BRIC Russia. With the looming spectre of a two-speed Europe on economic and monetary issues, there is a greater-than-ever need for the EU 27 to find greater unity and take common action in order to prevent the collapse of its common foreign policy.

## Chapter 1

# Russia's stagnation

In 2006 the highbrow pro-government Russian magazine *Ekspert* predicted that the ruble would become a global reserve currency and that Moscow would become one of the financial capitals of the world.<sup>3</sup> After the humiliations of the 1990s, an economic boom in the early 2000s brought confidence – and with it a more assertive foreign policy – back to Moscow. The Kremlin was convinced that Russia was once again a great power. In his 2007 state of the nation address, Putin himself declared that “not only has Russia fully overcome a long period of production decline, but it now ranks among the top ten economies in the world.”<sup>4</sup> The same year, Putin boasted to Europe that “historians will be the judge of what my people and I achieved in eight years. We re-established Russia’s territorial integrity, strengthened the state, moved in the direction of a multi-party system and re-established the potential of our armed forces.”<sup>5</sup>

However, economic turbulence has hit Russia almost as hard as it has the EU. In fact, in 2009 Russia saw GDP fall deeper than any other G20 state. By 2011, *Ekspert* was publishing articles on the spectre of looming stagnation.<sup>6</sup> Russia’s stability-obsessed elites were shaken by the vulnerability exposed by its economic overreliance on oil. One Russian minister confessed he realised during the 2009 crisis that “as soon as the markets tremble, the oil price falls and all our social problems come out as threats.”<sup>7</sup> The mood of the middle classes, the greatest winners of the BRIC-era and crucial for modernisation to succeed, is increasingly

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<sup>3</sup> See Mikhail Erschov, “Rublyami, pozhaluista”, *Ekspert*, 17 July 2006, available at [http://expert.ru/expert/2006/27/stremlenie\\_k\\_polnocennoj\\_konvertiruемости/](http://expert.ru/expert/2006/27/stremlenie_k_polnocennoj_konvertiruемости/).

<sup>4</sup> Vladimir Putin’s address to the Federal Assembly, 27 April 2007, available at <http://www.rg.ru/2007/04/27/poslanie.html>.

<sup>5</sup> G-8 Interview with Vladimir Putin, “I am a True Democrat”, *Spiegel Online International*, 6 April 2007, available at <http://www.spiegel.de/international/world/0,1518,486345-2,00.html>.

<sup>6</sup> See Tatyana Gurova, “Zadacha gosudarstvennoj vazhnosti”, *Ekspert*, 23 May 2011, available at <http://expert.ru/expert/2011/20/zadacha-gosudarstvennoj-vazhnosti/>.

<sup>7</sup> Unless otherwise stated quotations are from interviews with the authors.

pessimistic. This means that although Putin will return to the presidency in 2012, he will lead a different Russia than in his first two terms.

## Dreaming with BRICs

The Russian elite's pre-crisis hubris was based on a belief that the country had achieved a macro-economic breakthrough and would continue to grow on the back of high commodity prices and an expanding middle class. Taking at face value the 2003 Goldman Sachs report that grouped Russia with Brazil, China and India as the world's four largest emerging economies, Russian elites believed that their country could continue to grow rapidly until it caught up with the West.<sup>8</sup> They began to think that the Russian economy had decoupled from the West. In 2008, Putin boasted that Russia would overtake Britain and France in terms of GDP in 2009. Kremlin ideologues even argued that Russia now had the power and wealth to create an "East European Union", as a counterweight to the EU.<sup>9</sup>

Prosperity enabled Putin not only to consolidate his power but also to create a so-called Putin consensus.<sup>10</sup> Economically, he wanted foreign investors to be subordinate partners and was in favour of championing state corporations, especially in the energy sector. At the heart of this philosophy was the vision of Russia as an "energy superpower". The focus was not on diversifying the economy away from its reliance on oil but on how to turn these assets into political weapons. With this in mind, the government re-established control over most of the energy sector, created a rash of state corporations in sectors as diverse as banking or high-technology and limited foreign investment in "strategic sectors" of the economy. Russian authorities regularly bullied EU companies. For example, BP and Shell were forced to cede controlling stakes in the Sakhalin II and Kovytkva gas fields to Gazprom. Instead of courting economic partnerships with the EU, Russia ended up embroiled in trade disputes or bans with a dozen member states – and sought to dictate its energy agenda.<sup>11</sup>

Politically, the Putin consensus was centred on establishing a "vertical of power" – a code word for centralisation, with the government justifying the rolling back

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<sup>8</sup> Wilson and Purushothaman, "Dreaming With BRICs".

<sup>9</sup> Sergei Markov, "Chto b'iet po demokratii," September 2006, available at <http://dom.viperson.ru/wind.php?ID=499115&soch=1?17f1fd40>.

<sup>10</sup> See Ivan Krastev, Mark Leonard and Andrew Wilson (eds), "What Does Russia Think?," European Council on Foreign Relations, September 2009, available at [http://ecfr.eu/page/-/documents/ecfr\\_what\\_does\\_russia\\_think.pdf](http://ecfr.eu/page/-/documents/ecfr_what_does_russia_think.pdf).

<sup>11</sup> See Leonard and Popescu, "A Power Audit of EU-Russia Relations".



of civil liberties and regional autonomy by reference to foreign or internal threats. The regime increasingly defined itself against the West: it rejected Western norms by promoting the idea of “sovereign democracy”, which specified that Russia would pursue its own autonomous development. Moscow also capitalised on nostalgia for Soviet power: it promoted a partial rehabilitation of Stalin as an “effective manager” and honoured the KGB.<sup>12</sup> Putin described the collapse of the Soviet Union as “the greatest geopolitical catastrophe of the twentieth century”.<sup>13</sup>

Public approval of the Putin system was high because the regime was perceived as successful in delivering economic growth and restoring order and territorial integrity. Throughout the 2000s, Putin’s popularity ratings remained solidly high, peaking at 83 percent in October 2008, as the public credited his government with some of the highest living standards in Russian history and victory over the Chechen insurgency. There was widespread satisfaction during Putin’s presidency that the North Caucasus had been reintegrated into Russia and nationalists even called for further expansion. Putin was perceived as having won his war on terror whilst NATO sank into the Afghan quagmire.

Buoyed by domestic economic success, popularity and an assertive narrative, Putin’s foreign policy became gradually more aggressive. The Kremlin used gas cut-offs and pressure in Ukraine, cyber-attacks on Estonia, demanded the US withdraw from Central Asia and finally used military force in Georgia in order to assert what Medvedev called “a privileged sphere of interests” in the post-Soviet space.<sup>14</sup> Moscow adopted fiercely anti-American rhetoric – “Comrade Wolf knows whom to eat,” snarled Putin in a coded reference to the US in 2006 – and systematically wielded its veto against Western initiatives at the UN.<sup>15</sup> Meanwhile, it actively courted China, Venezuela and Iran. By 2008 relations had deteriorated into what many feared was a new Cold War. However, the financial collapse brought Russia’s hubris abruptly down to earth.

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<sup>12</sup> Svetlana Osadchuk, “Stalin makes a comeback with Russian teachers”, the *New York Times*, 31 August 2008, available at <http://www.nytimes.com/2008/08/31/world/europe/31iht-stalin.4.15773911.html>.

<sup>13</sup> Putin quoted in “Putin deplores collapse of USSR”, BBC News, 25 April 2005, available at <http://news.bbc.co.uk/1/hi/4480745.stm>.

<sup>14</sup> Andrew E. Kramer, “Russian Claims Its Sphere of Influence in the World”, the *New York Times*, 31 August 2008, available at <http://www.nytimes.com/2008/09/01/world/europe/01russia.html>.

<sup>15</sup> Philippe Naughton, “Putin takes swipe at hungry America’s ‘Comrade Wolf’”, the *Times*, 10 May 2006, available at <http://www.timesonline.co.uk/tol/news/world/europe/article715218.ece>.

## The end of dreams

The Russian government did not expect to be hurt by the market crash in 2008. As late as December 2008, Putin said that Russia would experience “minimal losses” from the financial crisis.<sup>16</sup> The Kremlin was “astounded” when Russia’s GDP shrank by 8.9 percent in 2009 – a deeper contraction than Greece in 2009 or 2010.<sup>17</sup> The Russian Central Bank spent a third of its reserves of \$600 billion in a costly attempt to prevent the fall of the ruble. The Russian stock exchange lost 80 percent of its value from peak to trough and oil lost 70 percent of its value, causing a budget deficit, before rebounding to over \$100 a barrel in 2011. Russia’s private sector was heavily leveraged to Western banks and found credit lines constrained. In retrospect, one leading Russian thinker says, the 2003 Goldman Sachs BRIC report was “one of the worst things that ever happened to Russia. That pamphlet convinced the elite that high oil prices would coast Russia to glory. When the crash happened, they saw their world collapse around them.”

The powerful Kremlin aide Vladislav Surkov says that “the main benefit of the last few years is we have taken a long sober look at ourselves”.<sup>18</sup> Moscow weathered the financial crisis, but it shattered illusions about its place in the world economy and caused a reassessment of the nation’s trajectory. Few Russian analysts now think that Russia is a major pole in the multipolar world and there is a new consensus that domestic renovation is urgently needed. “We thought we were rising with China, but now we know we are declining with the EU,” said one Kremlin-linked analyst. Rhetoric about being an “energy superpower” has been replaced by the need for diversification and foreign investment to sustain production and bring new hydrocarbon reserves online. “I never understood how dependent we were on raw materials and this made me talk about modernisation,” Medvedev said in 2010.<sup>19</sup> In short, post-BRIC Russia has realised that it is far from being self-sufficient. As a former Russian foreign minister explained: “In the future Russian foreign policy will be an extension of domestic renovation and this is only possible with investment, with technology – and these can only come from one place: the West.”

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<sup>16</sup> “Putin: Finance Crisis Will Cause Russia ‘Minimal Losses’”, *Deutsche Welle*, 5 December 2008, available at <http://www.dw-world.de/dw/article/0,,3852401,00.html>.

<sup>17</sup> Quote from Dmitry Medvedev’s speech at the Brookings Institution in 2010, available at [http://www.brookings.edu/events/2010/0413\\_medvedev.aspx](http://www.brookings.edu/events/2010/0413_medvedev.aspx); World Bank data available at <http://search.worldbank.org/data?qterm=Greece%20GDP%20growth&language=EN>.

<sup>18</sup> Vladislav Surkov quoted in Paul J. Saunders, “Russia’s Revised Strategic Plan”, New America Foundation, July 2011, available at <http://greatpowers.newamerica.net/sites/newamerica.net/files/policydocs/Saunders.%20Russia%20Strategy%20Outline%20Revised%20Draft%20Formatted%20PDF.pdf>.

<sup>19</sup> Dmitry Medvedev, “Russia-US Relations and Russia’s Vision for International Affairs”, Brookings Institution, 13 April 2010, available at [http://www.brookings.edu/events/2010/0413\\_medvedev.aspx](http://www.brookings.edu/events/2010/0413_medvedev.aspx).

In particular, the crisis shattered the illusion that Russia had achieved a macro-economic breakthrough. Russia's projected growth rate has fallen to 4.1 percent in 2011 and 3.7 percent for 2012 – lower than Moldova or Armenia, although still higher than most EU member states. Meanwhile, Russia's budget has expanded in the last five years to such an extent that the oil price would now have to be \$116 a barrel in order to balance it, thus increasing its vulnerability to fluctuations.<sup>20</sup> This has undermined confidence that the Russian economy was following the same trajectory as that of China and India. Russia could become more attractive to foreign investors if the West faces prolonged economic difficulties. However, one financial analyst suggests that even wealthy Russians do not think their investments are safe: "Western investors are keen to invest in Russia; the problem is that a lot of wealthy Russians refuse to invest here."

Growth is also being constrained by a governance crisis that has led economist Nouriel Roubini to describe the country as "more sick than BRIC".<sup>21</sup> The governance crisis is a consequence of the weak institutions, personalisation of power and fusion of property and power that defines Russian politics. There is an endemic problem of embezzlement of public funds and monopolistic behaviour by the Russian elite. Mismanagement and corruption at the top has seen a decline in public services – particularly in policing, safety standards, education, science and infrastructure. Putin recently acknowledged that as much as 80 percent of Kremlin orders to the regions are routinely ignored.<sup>22</sup> "Russia has not engaged in capacity building but incapacity hiding," says Ivan Krastev.

Thus instead of modernising during the Medvedev presidency, Russia has mostly declined on indexes that measure corruption, property rights, ease of doing business or competitiveness (see Figure 1). In 2010, Russia was as corrupt as Papua New Guinea, with the property rights of Kenya, as easy to do business in as Uganda and as competitive as Sri Lanka. This sense of decay has compounded the problem of capital flight from Russia, forecast at \$50 billion for 2011 by Russian authorities. Much of this is leaving in relatively small sums only attributable to individual transfers.<sup>23</sup>

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<sup>20</sup> "Kudrin Sees Threat From Pensions and Oil", the *Moscow Times*, 14 September 2011, available at <http://www.themoscowtimes.com/mobile/article/kudrin-sees-threat-from-pensions-and-oil/443678.html>.

<sup>21</sup> Nouriel Roubini, "Another BRIC in the Wall?", *Project Syndicate*, 15 October 2009, available at <http://www.project-syndicate.org/commentary/roubini18/English>.

<sup>22</sup> David Hearst, "Putin: we have lost Russia's trust", *Guardian*, 12 November 2011, available at <http://www.guardian.co.uk/world/2011/nov/12/putin-russia-lost-trust>; and Andrew Monaghan, "The Russian *Vertikal*: the Tandem, Power and the Elections", Chatham House, Russia and Eurasia Programme Paper REP 2011/01, June 2011, available at [http://www.chathamhouse.org/sites/default/files/19412\\_0511ppmonaghan.pdf](http://www.chathamhouse.org/sites/default/files/19412_0511ppmonaghan.pdf).

<sup>23</sup> Darya Korsunskaya, "Russia raises 2011 capital flight forecast to \$50 bln", *Reuters*, 5 October 2011, available at <http://www.reuters.com/article/2011/10/05/russia-outflow-idUSL5E7L51WL20111005>.

**Figure 1**

*Russia's place in the world*

<b>GLOBAL INDEX</b>	<b>RUSSIA'S GLOBAL RANKING</b>	<b>JUST BEHIND...</b>
<b>Billionaires</b>	3	China
<b>Global Competitiveness</b>	66	Vietnam
<b>Human Development Index</b>	66	Belarus
<b>Failed State Index</b>	82	Algeria
<b>Property Rights</b>	130	Bosnia and Herzegovina
<b>Infrastructure Quality</b>	100	Mali
<b>Air Travel Quality</b>	105	Nigeria
<b>Bribery</b>	114	Mongolia
<b>Quality Corporate Boards</b>	123	Egypt
<b>Ease of Doing Business</b>	120	Cape Verde
<b>Police Reliability</b>	132	Mauritania
<b>Life Expectancy</b>	135	Pakistan
<b>Press Freedom</b>	140	Ethiopia
<b>Corruption Perception</b>	154	Papua New Guinea

Source: Transparency International Corruption Perception Index (2010); United Nations (2005-2010); World Economic Forum Global Competitiveness Report 2011–2012.

Putin's return is set to further Russia's governance crisis by further personalising and de-institutionalising power, while frustrating the ambitions of a younger generation of politicians. Russia now faces serious economic and social challenges that will threaten growth prospects and stability in the medium term and will require good governance to overcome. Russia is in chronic need of new infrastructure and modernised industrial stock. Despite its desire for increased investment, the Russian government's poor provision of social goods and endemic corruption discourages investors and hampers productivity. Of particular importance, oil production, which increased dramatically during the 2000s, will stagnate over the next 10 years. "The gap between rhetoric and reality is widening," says one Russian journalist.

## Same Putin, different Russia

Beyond Moscow, the combination of Russia's economic and governance crisis has undermined the public's faith in the regime, which is increasingly seen as unsuccessful in managing the economy, fighting corruption or controlling the North Caucasus. In 2009 more representatives of the Russian state were killed in the North Caucasus than US servicemen in Iraq.<sup>24</sup> Chechnya is increasingly viewed as a de facto independent state with control of its own army and the ability to blackmail Moscow. "If Russia is lucky, Chechnya will secede," jokes one Russian analyst. "If not, Russia won't be able to secede from Chechnya." Many nationalists and liberals are now questioning the merits of a Russian Chechnya. Uncontrolled mass migration from the Caucasus and Central Asia has seen a rise in Russian nationalism, which has mutated from expansionist to exclusivist. The increasingly popular campaign movement "Stop Feeding the Caucasus" is pushing for scarce funds to be spent renovating the rest of Russia and is widely seen as code for letting the North Caucasus go.

In fact, together with events such as forest fires and race riots, the economic turmoil has exposed the governance crisis to the public. Opinion polls have shown a steep decline in support for United Russia, Putin's party, and a population increasingly pessimistic and angry about corruption. Putin's popularity is now in decline: only 47 percent of Russians found him "trustworthy" in November 2011 compared to 69 percent in late 2009.<sup>25</sup> The majority now believe the country is more corrupt than in the 1990s.<sup>26</sup> But although dissatisfaction is widespread, it has not yet produced meaningful opposition. Rather, it has translated into a rise in emigration: 22 percent of the population would like to leave and the national audit chamber has estimated that 1.25 million people have left the country in the past few years.<sup>27</sup> Worryingly for the regime, the most alienated are the greatest winners of the Putin era: the middle classes. These factors have put under strain the "Putin consensus" of the last decade and contributed to a foreign-policy rethink.

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<sup>24</sup> In 2009 the number of US soldiers killed in Iraq was 150, while more than 250 Russian police officers and soldiers died in the north Caucasus. Figures available at [http://www.globalsecurity.org/military/ops/iraq\\_casualties.htm](http://www.globalsecurity.org/military/ops/iraq_casualties.htm) and <http://en.rian.ru/russia/20100116/157570882.html>.

<sup>25</sup> Poll conducted by the Public Opinion Foundation, available at [www.fom.ru](http://www.fom.ru); Charles Clover, "Rising chorus of boos greets Russia's rulers," *Financial Times*, 24 November 2011, available at: <http://www.ft.com/cms/s/0/015176aa-1689-11e1-bc1d-00144feabdco.html#axzz1ef8JvJVn>

<sup>26</sup> Poll conducted by the Levada centre. For more information see [www.levada.ru](http://www.levada.ru).

<sup>27</sup> Pavel Kanygin, "Russia. Dislike," *Novaya Gazeta*, 1 June 2011, available at <http://en.novayagazeta.ru/society/8641.html>.

**Figure 2**  
*Perceptions of Russian society*

PERCENTAGE	PERCEPTION
67	Feel nervous of the police
62	Fear the impoverishment of the population
58	Do not feel protected by the law
56	Ethnic clashes will definitely or probably occur
52	Theft and corruption are higher than in 1990s
50	Disapprove of the Russian government
26	Believe Putin has successfully or adequately coped with Russia's problems
22	Want to emigrate
9	Actively thinking or preparing to emigrate
1	Believe official's income declarations

Source: Levada Centre, 2011.

The realisation that Russia is not a BRIC after all has forced Moscow to pursue a more cautious and pragmatic foreign policy – somewhat like during Putin’s first few years as president when the country last felt it was economically weak. It has scaled down the anti-Western foreign policy of Putin’s second presidency, when it sought to push the US and the EU out of the post-Soviet space and blocked Western initiatives at the UN. Russia has been more co-operative on Iran and abstained from vetoing the resolution authorising NATO involvement in Libya. But Russia also sees the EU as being in decline and therefore wants to build a partnership on an equal footing to manage such a double decline and to prevent the emergence of a world dominated by China and the United States.<sup>28</sup> Russian threat perceptions and foreign policy in its “near abroad” are also changing. Moscow has a new approach to the post-Soviet space – traditionally the theatre of Western-Russian strategic rivalry. As one Russian analyst puts it: “Russia today wants to rebuild its empire but does not want to pay for it. This is our challenge.”

<sup>28</sup> Sergei Karaganov, Timofei Bordachov and Fyodor Lukyanov, “Towards an Alliance of Europe”, Analytical Report by the Russian Group of the Valdai International Discussion Club, available at <http://vid-1.rian.ru/ig/valdai/Alliance%20eng.pdf> (hereafter, Karaganov, Bordachov and Lukyanov, “Towards an Alliance of Europe”).

## *Chapter 2*

# Russia's lily-pad empire

In August 2008 – less than a month before the collapse of Lehman Brothers triggered a global financial meltdown – Russian troops celebrated their swift military victory over Georgia by watching a classical music concert from the tops of their tanks in the ruins of Tskhinvali, the South Ossetian capital. Elsewhere, post-Soviet, European and American elites were nervously debating where Russia would intervene next and feared that it might be in Ukraine's Crimea. But two years later, in June 2010, Russia did not even send troops to Kyrgyzstan as Bishkek requested when the country descended into ethnic riots. Moscow's newfound restraint in Kyrgyzstan illustrates the new approach it has taken to its “near abroad” since the economic crisis.

After the collapse of the Soviet Union, Moscow deployed heavy economic, military and political resources to transform its former empire into a sphere of influence. Yet despite strenuous efforts to control this space, Russia's influence in the region has been eroding over the last decade. To counteract this, Russia has been developing a more streamlined strategy to maintain influence in the region. Russia has increasingly relied on power projection rather than full control, owning key economic assets rather than splashing around subsidies, and focusing its integration efforts primarily on a “core” of Belarus, Kazakhstan and Ukraine. Elsewhere, Moscow has contented itself with a light-footprint “lily-pad empire” of pipelines, military bases and key chunks of the economy.

## The eroding empire

Russian elites believe that the country's great-power status depends largely on the role it plays in the post-Soviet space – it can only be a pole in a multipolar world if it has a sphere of influence. “Without it we are just a big state,” says one Russian analyst. There also is a deep sense of entitlement to the post-Soviet

states – as betrayed by Putin’s casual remark that the Soviet Union was in essence “Russia, but just under a different name”.<sup>29</sup> While accepting that the Baltics had been “lost”, Russia subsidised other post-Soviet economies through cheap energy and preferential tariffs, maintained a visa-free zone, allowed mass labour migration and sponsored numerous reintegration projects. These included the Commonwealth of Independent States (CIS) as the post-Soviet umbrella organisation and also used smaller groupings such as the economic Eurasian Economic Community, Single Economic Space and the Collective Security Treaty Organisation (CSTO).<sup>30</sup> Moscow also maintained a military presence in several ex-Soviet states – sometimes against their will – and used trade embargoes and its oil and gas transit monopoly as leverage. In this way, Russia remained the regional hegemon, limiting the sovereignty and curtailing the foreign-policy choices of other post-Soviet states.

Throughout the 2000s, Russia continued its economic or security support for the CIS states, but systematically asked for concrete concessions, such as control of countries’ strategic assets, rather than just assurances of brotherly love. Simultaneously, Moscow began to put greater pressure on those who ventured to drift away from its orbit, such as Ukraine after the 2004 Orange Revolution. Russia’s coercive attempts to dominate the CIS culminated in the 2008 war with Georgia, but the war demonstrated not so much Russian power as its limitations. One Russian expert summed up: “Before 2008 we had a ‘Yes, we can!’ attitude to the CIS. But in the war with Georgia we discovered that ‘it’s all we can.’”

The CIS has become increasingly irrelevant. “The CIS is a useless gathering – a chance to exchange a few jokes and drink vodka,” said the foreign minister of a participating state. Thus, paradoxically, Yeltsin’s “weak” Russia was more dominant in the CIS in the 1990s than Putin’s “strong” Russia in the 2000s. Since 2008, post-BRIC Russia has increasingly found that it is no longer the only anchor of the post-Soviet space. The West has become more engaged in Eastern Europe and the South Caucasus, while China and the US have constrained Russian ambitions in Central Asia. The post-Soviet countries have also grown wary of Moscow’s dominance and have come up with strategies to balance Russia’s pressure and decrease their dependence on it.

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<sup>29</sup> Interview by Putin on the three federal TV channels, 18 November 2011, available at <http://www.vg-news.ru/news-intervyu-putina-trem-federalnym-kanalam-polnyi-tekst>.

<sup>30</sup> Only Turkmenistan did not have a visa-free regime with Russia (and most of the other CIS countries). Russia also requires visas from the citizens of Georgia.



The EU has grown into an important player in Russia's neighbourhood: in 2003, it launched the European Neighbourhood Policy (ENP), later regionally rebranded as the Eastern Partnership (EaP). Its aim was to help transform the six states in the European part of the post-Soviet space – Armenia, Azerbaijan, Belarus, Georgia, Moldova and Ukraine – into well-governed market democracies. This is “enlargement-lite”: the EU offers assistance to its eastern partners in exchange for deep political, economic and social reforms, without ever promising EU membership as a reward. Since then, the EU has become more present in the region's economies: it has now overtaken Russia as the main trading partner of all these countries except for Belarus. Kyiv and Brussels are close to finalising a deep and comprehensive free trade agreement (DCFTA) that could tie Ukraine even closer to the EU; Moldova and Georgia will start negotiations soon.

The EU has also increased its profile as a security actor and has begun to play a more active role in the management of protracted conflicts in the region. Brussels is now a mediator in talks over Transnistria and has a border assistance mission in Ukraine and Moldova and a monitoring mission in Georgia. When President Medvedev invited the EU to develop a new pan-European security agreement, the EU, under Angela Merkel's leadership, made it clear that any agreement was conditional on progress in resolving the Transnistria conflict. And while little headway has been made, the EU's role reduces Russia's own room for manoeuvre in Moldova or Georgia. Although the EU itself struggles to turn its growing economic and security presence in the region into political power, it has already managed to constrain Russia's options in the region.

**Figure 3***Trade patterns in the Eastern Partnership*

<b>EAP COUNTRY</b>	<b>EU 27'S SHARE OF TRADE</b>	<b>RUSSIA'S SHARE OF TRADE</b>	<b>TURKEY'S SHARE OF TRADE</b>
<b>Armenia</b>	32.1 (1st place)	20.8 (2nd)	4.4 (6th)
<b>Azerbaijan</b>	46.9 (1st)	7.4 (3rd)	8.2 (2nd)
<b>Belarus</b>	25.1 (2nd)	48.2 (1st)	0.6 (10th)
<b>Georgia</b>	31.7 (1st)	4.4 (7th)	15.6 (2nd)
<b>Moldova</b>	52.3 (1st)	12.3 (3rd)	4.8 (4th)
<b>Ukraine</b>	31.4 (1st)	28.2 (2nd)	4.0 (4th)

Source: DG Trade, European Commission

Meanwhile, in Central Asia, Russia now has to compete with China, whose economic and political presence in the region has grown dramatically. In 2010, China's overall trade with the five Central Asian states totalled €23 billion – more than that of the EU or Russia.<sup>31</sup> China is now the primary source of foreign investment for the five states; only Uzbekistan still trades more with Russia than with China.<sup>32</sup> Central Asia makes up 10 percent of China's gas and oil needs (up from 5 percent a few years ago) and Beijing is developing oil and gas fields in Kazakhstan, Turkmenistan and Uzbekistan.<sup>33</sup> Chinese-built infrastructure is reducing Central Asia's dependency on Russian transport links: Beijing has joined forces with Ashgabat, Tashkent and Astana to build a network of pipelines to transport hydrocarbons eastward, breaking Moscow's monopoly over the region's energy transit and thus reducing Russian leverage. Backed by Chinese loans, Central Asian governments and Chinese companies are building roads in Tajikistan and Kyrgyzstan and a high-speed train connection between Almaty and Astana. One Chinese government advisor says that Russia will have to "accept the new reality" that it is "no longer the hegemon in Central Asia".

<sup>31</sup> "China Analysis: The new Great Game in Central Asia", European Council on Foreign Relations and Asia Centre, 6 September 2011, available at: [http://www.ecfr.eu/page/-/China%20Analysis\\_The%20new%20Great%20Game%20in%20Central%20Asia\\_September2011.pdf](http://www.ecfr.eu/page/-/China%20Analysis_The%20new%20Great%20Game%20in%20Central%20Asia_September2011.pdf) (hereafter, "China Analysis: The new Great Game in Central Asia").

<sup>32</sup> See DG Trade Statistics, available at <http://ec.europa.eu/trade/creating-opportunities/bilateral-relations/statistics/>.

<sup>33</sup> "China Analysis: The new Great Game in Central Asia".

However, while the Central Asian states welcome the opportunity to diversify their trade away from Russia, they are also wary of China. According to a recent poll, an overwhelming majority of Kyrgyz and Kazakhs saw Russia as a friend and China as a threat.<sup>34</sup> In the aftermath of the ouster of President Bakiyev last year, people in Bishkek looted Chinese, not Russian, shops.<sup>35</sup> In Kazakhstan and Tajikistan, the news about the possible lease of land to Chinese farmers sparked anti-government protests. Despite such wariness in Central Asia, the lures of economic and political benefits of a partnership with China are irresistible and are increasingly constraining Russian power.

Other actors such as the US (which has a presence in Central Asia because of the war in Afghanistan) and Turkey (which has an economic and political presence in the South Caucasus and to some extent in Central Asia) have further eroded Russian dominance in the region. Taken together, Beijing, Brussels, Ankara or Washington have provided the post-Soviet states with alternative sources of political legitimacy, loans, investment and security partnerships, which they readily used to expand their foreign-policy options and move a step away from Russia's orbit. And while none of the other powers is vying to replace Russia, their increasing influence in the region has already undermined its role as regional hegemon.

## An empire on the cheap

There remains a widespread consensus in Russian society and the political elite that Moscow should strive to retain influence throughout the post-Soviet space. The "liberal end" of Russia's political spectrum is not much different from the hardliners in this respect: the Institute of Contemporary Development (INSOR), a think tank that had even called for Russia to join NATO, argued in a recent study that Russia should have a right to intervene in CSTO states without the consent of all the bloc's members.<sup>36</sup> But Russian elites are increasingly torn between this desire to retain a sphere of influence and the rising economic and political costs which this ambition entails. Even Russian officials now agree that "complete integration of the CIS is impossible".<sup>37</sup>

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34 "Sun Zhuangzhi, "An analysis of tension points and security trends in Central Asia", *Xinjiang Shifandaxuexuebao*, volume 32, number 2, March 2011.

35 Qin Jize, "Kyrgyz violence hurting business", *China Daily*, 22 June 2010, available at [http://www.chinadaily.com.cn/bizchina/2010-06/22/content\\_10001938.htm](http://www.chinadaily.com.cn/bizchina/2010-06/22/content_10001938.htm).

36 Vladimir Socor, "Medvedev-led think tank proposes reinforcing Russia-led CSTO", *Eurasia Daily Monitor*, volume 8, issue 164, 8 September 2011, available at [http://www.jamestown.org/single/?no\\_cache=1&tx\\_ttnews%5Btt\\_news%5D=38373](http://www.jamestown.org/single/?no_cache=1&tx_ttnews%5Btt_news%5D=38373).

37 Remarks by Grigory Karasin, Deputy Secretary of the Russian Ministry of Foreign Affairs, at an International Institute for Strategic Studies (IISS) event in London, 1 July 2011.

The first attempts to balance the costs and benefits of running a sphere of influence were undertaken under the slogan of foreign-policy “economisation” during Putin’s first term. In particular, Gazprom increased prices for gas supplied from Russia to almost all of its post-Soviet consumers. Since the economic crisis, Moscow has become even less enthusiastic about throwing money at the “near abroad” without clear returns. “Russia is no longer going to be a humanitarian superpower in the CIS giving out pensions like in the 1990s,” says one Russian diplomat.

Diminished economic expectations at home and the increased presence of other actors in the region have seen Moscow scale back its ambitions and craft a post-BRIC strategy for the post-Soviet space. Russia has accelerated its foreign-policy “economisation” as it aims for a lower-cost sphere of influence. It is deploying limited resources selectively to rebuild the region into a kind of “lily-pad empire” somewhat like the “lily-pad military” proposed by former US Defence Secretary Donald Rumsfeld.<sup>38</sup> Instead of large quasi-permanent US military bases, Rumsfeld argued for smaller, “lily-pad” deployments in strategic locations which would enable the US to project power and quickly deploy forces when necessary. In its version of a “lily-pad” empire, Russia seeks to get the benefits while minimising the costs. As one Russian expert says: “We would like to choose the best bits of the CIS” – that is, energy infrastructure, key sectors of the economy and the right to station our military bases abroad – “and leave the rest to go to hell.”

Energy politics is a key element of this “lily-pad” empire. Gazprom has majority stakes in gas transit networks in Armenia and Moldova, and just recently gained control of Belarus’ gas transit system in exchange for loans and cheaper gas prices for Minsk. These “energy footholds” provide Russia with leverage over the transit states. Russia also hopes to buy into Ukraine’s gas pipelines network – in the latest spat between Moscow and Kyiv about the 2012 gas prices, Russia is eyeing a gradual takeover of Ukraine’s national energy champion Naftogaz.<sup>39</sup>

Alongside energy, military force is the other key element that underwrites the “lily-pad” empire. Moscow’s overseas deployments are far from transparent, but according to some estimates, Russia has at least 34,000 servicemen stationed in the post-Soviet space (see Figure 4). In 2010, Russia reached an agreement

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<sup>38</sup> See more in Catherine Lutz (ed.), *The Bases of Empire: The Global Struggle against US Military Posts*. London: Pluto Press, 2009.

<sup>39</sup> Alexander Gabuev, Vladimir Soloviev and Dmitri Belikov, “Ukraina s odnogo gaza ne ponimayet”, *Kommerstant Ukraine*, 12 August 2011, available at <http://kommersant.ru/doc/1750227>.

**Figure 4**  
*Russian military bases in the CIS*

<b>HOST COUNTRY</b>	<b>TYPE OF MILITARY PRESENCE</b>	<b>APPROXIMATE NUMBER OF RUSSIAN SERVICEMEN</b>
<b>Armenia</b>	Air base in Yerevan, military base in Gyumri (originally until 2020, in 2010 extended until 2044)	4,000
<b>Azerbaijan</b>	Radar station in Qabala (lease to expire in 2012, negotiations on the extension ongoing)	900
<b>Belarus</b>	Radar station in Baranovichi, naval communications centre in Vileyka	2,000
<b>Georgia</b> (opposed by government)	Military base in Abkhazia and South Ossetia	7,000–9,000
<b>Kazakhstan</b>	Radar station in Balkhash, Baikonur station	Unknown
<b>Kyrgyzstan</b>	Airbase in Kant, naval training and research centre at Issyk-Kul	500–700
<b>Moldova</b> (opposed by government)	Transnistria “operational group”	1,500 (including 500 peacekeepers, 2003 deadline for withdrawal missed)
<b>Tajikistan</b>	Military base (motorized rifle regiments in Dushanbe, Kulyab, Kurgan-Tyube and helicopter squadron in Aini)	5,500
<b>Turkmenistan</b>	None	n/a
<b>Ukraine</b>	A naval base including radar station in Sevastopol and the Black Sea Fleet (in 2010 extended until 2042)	13,000
<b>Uzbekistan</b>	None – Tashkent refused Russia’s offer to open an air base in 2007	n/a

Source: International Institute for Strategic Studies Military Balance 2010.

with Ukraine to extend the lease for its military base in Crimea until 2042 in exchange for a 30 percent discount on the price of gas for 10 years.<sup>40</sup> Armenia also recently extended the lease for a Russian base on its territory until 2044. However, rising costs and domestic constraints at home mean that Russia now seems to be calculating the costs and benefits of its military endeavours: the era of “eat-all-you-can” military policy in the CIS seems to be closing. Although Russia already had a small military base in Kyrgyzstan, it did not think it was worth stabilising its ally in 2010. As one Russian expert put it: “If it goes wrong, our bases are out; if it goes right, we’re there forever.”

Russia’s new streamlined approach to the “near abroad” is made possible in part due to a belief that the West is a rather half-hearted and “lazy” competitor.<sup>41</sup> Moscow is aware that the EU has lost its appetite for further enlargement eastward and that the US is less enthusiastic about supporting “colour revolutions” in the post-Soviet space. Sucking fewer resources, a “lily-pad” presence allows Russia to use it as leverage over local partners if the need arises – a “tripwire” to maintain the status quo.

## Empire-lite vs. enlargement-lite

In his first major policy initiative since announcing his intention to return to the presidency in 2012, Putin called for a Eurasian Union – a nucleus of post-Soviet reintegration centred around the Customs Union of Russia, Belarus and Kazakhstan.<sup>42</sup> His vision is bound to clash with the EU’s own “enlargement-lite” neighbourhood policy. The first skirmish is already taking place over Ukraine. Putin warned that if Ukraine refused to join the Customs Union and signed the DCFTA with the EU instead, Russia would respond by measures preventing Ukrainian exports from “flooding the Russian market”.<sup>43</sup> Moscow sees it as a binary choice: one Kremlin source said that “the time has come for Kyiv to choose – either you are with us or with Europe. You cannot sit on two chairs.”<sup>44</sup>

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<sup>40</sup> The deal costs Russia an estimated \$40 billion. For more on the deal and its implications, see James Sherr, “The Mortgaging of Ukraine’s Independence”, Chatham House briefing paper, August 2010, available at [http://www.chathamhouse.org/sites/default/files/public/Research/Russia%20and%20Eurasia/bpo810\\_sherr.pdf](http://www.chathamhouse.org/sites/default/files/public/Research/Russia%20and%20Eurasia/bpo810_sherr.pdf).

<sup>41</sup> The authors would like to thank Stanislav Scerieru for suggesting this term.

<sup>42</sup> Putin quoted in “New Integration Project For Eurasia: the future being born today”, *Izvestia*, 3 October 2011, available at <http://www.izvestia.ru/news/502761>.

<sup>43</sup> “Putin pushes for customs union in visit to Kiev”, *New Europe*, 17 April 2011, available at <http://www.neurope.eu/article/putin-pushes-customs-union-visit-kiev>.

<sup>44</sup> Vladimir Solovyov, “Viktor Yanukovich popadayet pod perekriostniy priem”, *Kommersant*, 22 September 2011, available at <http://www.kommersant.ru/doc/1778537>.

The EU and Moscow continue to have quite different visions in a number of policy areas. Moscow opposes the EU's offer of economic integration with all EaP countries, which would further dilute Russia's own economic influence. In energy terms, the EU is proposing to its eastern partners the "unbundling" of companies' energy production assets and ownership of transmission networks just when Russia is trying to consolidate control over key energy infrastructure in the region. Moldova and Ukraine are both members of the European Energy Community and are required to implement relevant parts of the EU's energy *acquis* – including unbundling of their energy sectors – by 1 January 2015. This is already ruffling Moscow's feathers. In addition, the projected construction of an EU-backed Trans-Caspian pipeline which Russia opposes is another worry for Moscow.

However, the game between the EU and Russia in the post-Soviet space is not entirely zero-sum. There could be opportunities for co-operation over conflict settlement in Moldova, trade liberalisation with Ukraine or mutual efforts to stabilise Central Asia, where Russia's changing threat perceptions may turn into opportunities. The EU's primary objective, like that of Russia, is maintaining stability. The EU can co-operate with Russia – and also with China and the US – to promote economic development in the region and enhance security. At the same time, however, the EU is increasingly competing with China and Russia for access to the region's energy. Moscow's posture in the region is gradually being shaped by China – the relationship that will increasingly define the way Russia engages with Europe in this area and beyond.





## *Chapter 3*

# The closing of Russia's China option

In the corridors of one of China's most powerful think tanks, a joke has been going around about Russia. The leaders of the BRIC countries each go in turn to God to ask when their currency will be a reserve currency and they exit in tears. God tells them all that they would not live to see renminbi, rupees and reals as global reserve currencies. Yet Medvedev comes out puzzled. When asked what happened, he tells them that God burst into tears: even he would not live to see the ruble as a reserve currency. The joke illustrates the Chinese foreign policy establishment's view of Russia's claim to be a BRIC.

The relationship with China is of existential importance to Russia. Managed well, its commodity economy could be pulled along by a juggernaut of Asian demand. Moscow also needs China in order to fulfil its long-term energy and geopolitical ambitions. Yet the Russian imagination is also haunted by the spectre of losing its Far East to China. Russia knows that unless it modernises, it could find that the resources and politics of the region effectively are controlled by China. In short, China has become Russia's indispensable nightmare. Whereas before the crisis Russia and China were joined in a partial anti-Western entente, Moscow now finds itself at best in the problematic position of junior partner.

## A counter-hegemonic bloc

In the 2000s, Russia and China were brought together by a vehement dislike of American hegemony. The interventions in Afghanistan and Iraq, NATO deployments across Central Asia and the "coloured revolutions" convinced both powers that they had a common cause in what Putin and Jiang

Zemin called “defying hegemonism”.<sup>45</sup> To achieve this, Moscow and Beijing established forums that excluded the West such as the BRIC summits, launched in Yekaterinburg in 2009, and the Shanghai Cooperation Organisation (SCO). It hoped to use such forums to force the US to withdraw from Central Asia, prevent democratic revolutions, and use an unofficial “veto entente” at the UN. Russia imagined that together it and China could form a counter-hegemonic bloc that would dilute US unipolarity. Russia hoped that it could balance between the US and China if relations soured, while benefitting from being courted by both. A confident Moscow saw no reason to fear a country that had long been the junior partner of Soviet or Tsarist Russia.

Russia thus imagined a series of strategic China “options”. Economically, Russia thought its trade relationship with Beijing made Europe less vital: the mutual trade expanded from \$14 billion to over \$55 billion from 2003 to 2010, with China replacing Germany as Russia’s biggest trade partner in 2010.<sup>46</sup> The Kremlin had high hopes for growth in oil and gas exports to China, hoping it could blackmail the EU by threatening to divert flows to the Pacific. The energy relationship between China and Russia seemed the perfect match of the world’s largest oil producer and second-largest consumer. In the 2000s, Russian power in negotiations increased as energy prices rose alongside Chinese consumption. Talks began in earnest about major gas exports and Russia agreed to its first China-bound pipeline, a spur of the East Siberia-Pacific Ocean (ESPO) in 2003, with deliveries starting this year.

Militarily, Russia envisaged Chinese arms imports creating a long-term strategic partnership. Russia supplied Beijing with state-of-the-art equipment that enabled China to put a man in space, begin an aircraft carrier programme and develop stealth fighters.<sup>47</sup> This relationship raised eyebrows in the West: the US estimated that the overwhelming majority of China’s imported military hardware has Russian origins.<sup>48</sup> During the mid-2000s, the value of these purchases rose above \$2 billion per annum – almost 63 percent of Russian arms exports in 2005.<sup>49</sup> But although

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45 Jiang Zemin and Vladimir Putin jointly committed to “defying hegemonism” in the 1999 Beijing Declaration which paved the way for a deepening Sino-Russian rapprochement. See “China, Russia issue Beijing declaration”, available at <http://bg.chineseembassy.org/eng/dtxw/t131515.htm>.

46 “China, Russia set for record trade year”, *China Daily*, 22 September 2003, available at [http://www.chinadaily.com.cn/en/doc/2003-09/22/content\\_266221.htm](http://www.chinadaily.com.cn/en/doc/2003-09/22/content_266221.htm); Jack Perkowski, “The Russian Bear And The Chinese Dragon”, *Forbes*, 29 September 2011, available at <http://www.forbes.com/sites/jackperkowski/2011/09/29/the-russian-bear-and-the-chinese-dragon/>.

47 “China’s first aircraft carrier: From Russia with love”, the *Guardian*, 11 August 2011, available at <http://www.guardian.co.uk/commentisfree/2011/aug/11/china-aircraft-leader>; Thomas Grove, “New Chinese stealth jet starts talk of Russian help”, *Reuters*, 18 August 2011, available at <http://www.reuters.com/article/2011/08/18/us-russia-china-jet-idUSTRE77H1AZ20110818>.

48 Bobo Lo, *Axis of Convenience*. London: Brookings Institution and Chatham House, 2008, p. 79.

49 See SIPRI Arms Transfers Database, available at <http://www.sipri.org/databases/armstransfers>.

security ties became thicker, they remained frosty: Russia never supplied its most advanced technology to China and mutual suspicions were never fully overcome.

Thus, although the relationship between China and Russia became closer, it never evolved into a true strategic partnership. Russian diplomacy never overcame suspicion of Beijing. According to a leaked US embassy cable from 2007, “the Chinese Embassy expressed frustration at the lack of follow-through on the seemingly impressive number of bilateral agreements already in place, blaming Russia’s inherent suspicion of Chinese economic power, as well as increasing Chinese self-sufficiency in areas such as weaponry”.<sup>50</sup> Thus, according to one European diplomat, although Russia enjoys relatively good access to Chinese policymakers, it “does not seem to get much out of the relationship”. As an American diplomat in Beijing puts it: “Russia-China relations are a hollow pyramid: they are great at the top with very little underneath.”

## The chill of China’s shadow

China is no longer an emerging market but an emerging superpower that no longer needs Russia as much as it did a few years ago. Post-BRIC Russia now feels it is being overtaken by a historically weaker neighbour with which it shares a 4,195 km-long border that is mostly composed of former Chinese territory. The geopolitical pressure that brought Russia and China together has also eased as a multipolar world has emerged, NATO is set to withdraw from Central Asia and the West is in economic disarray. The US-Russia “reset” has also strained relations between Beijing and Moscow. For example, the Chinese were annoyed by Russia’s abstention in the vote in the UN Security Council authorising military intervention in Libya in March. “Russia did not behave like a reliable partner,” said a leading Chinese analyst affiliated to the government. “They always used to be on the frontline against the US but have retreated.”

Economic relations between the two countries are still growing but they are increasingly imbalanced: although China became Russia’s largest trade partner in 2010, Russia provided only 2 percent of China’s imports and bought only 1.9 percent of its exports.<sup>51</sup> This means that China trades more with Singapore or the

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<sup>50</sup> “Chinese Premier Wen Visits Moscow; Focus on Economics and Energy”, Daily Telegraph, 31 January 2011, available at <http://www.telegraph.co.uk/news/wikileaks-files/bp-wikileaks/8294137/CHINESE-PREMIER-WEN-VISITS-MOSCOW-FOCUS-ON-ECONOMICS-AND-ENERGY.html>.

<sup>51</sup> See EU Commission DG Trade statistics database, available at [http://trade.ec.europa.eu/doclib/docs/2006/september/tradoc\\_113366.pdf](http://trade.ec.europa.eu/doclib/docs/2006/september/tradoc_113366.pdf).

Netherlands than with neighbouring Russia. Moscow's share of China's imports has more than halved since 1992. Beyond big energy deals, small and medium enterprise trade is hampered by the poor Russian business climate. "We are frustrated that Russia blocks investments in certain sectors, harasses traders in Siberia and is too corrupt to operate in," says one Chinese analyst, echoing many EU concerns.

Russia's energy partnership with China is also less promising than it once appeared to be. In 2010, Chinese oil imports from Russia were only 7.5 percent of the total – below Angola, Oman and Iran.<sup>52</sup> In 2009, Asia accounted for only 12 percent of Russia's total crude oil exports.<sup>53</sup> The 2009 oil price crash saw Russia's energy clout in negotiations undermined. China skilfully used Russia's moment of need to get cheap oil. At the onset of the credit crunch, Moscow urgently needed funds to progress on the China-bound spur of the East Siberia-Pacific Ocean pipeline.<sup>54</sup> This gave China an opportunity. Russia's state pipeline and oil companies Transneft and Rosneft took a \$25 billion dollar loan in 2009, locking them into a long-term contract at below market rates for oil. "The financial crisis unlocked the Russian oil fields for us," says one Chinese analyst. But by 2011 Rosneft and China National Petroleum Corporation had already locked horns over the deal, with Moscow accusing Beijing that it underpaid billions of dollars for oil supplies.<sup>55</sup>

Russia's high hopes about exporting gas to China remain unfulfilled. China's new five-year plan does provide for an energy- and gas-intensive China, which could increase reliance on Russia. But although Moscow has agreed in principle to supply gas to China, talks remain deadlocked. Russia has been frustrated by tough Chinese negotiators who have succeeded in securing prices that are lower than those for gas supplied to Europe. Some Chinese analysts are now calling for Beijing to walk away from the troubled gas negotiations with Russia altogether because of the shale-gas revolution and new options in Central Asia.<sup>56</sup> China has also broken the Russian pipeline monopoly from Central Asia, weakening its regional influence.

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<sup>52</sup> US Energy Information Administration, available at <http://www.eia.gov/countries/cab.cfm?fips=CH>.

<sup>53</sup> This will rise with ESPO. For more information see the US Energy Information Administration, available at <http://www.eia.gov/>.

<sup>54</sup> This is the same pipeline that anti-corruption activist Alexey Navalny claims a \$4 billion fraud was committed on.

<sup>55</sup> "Russia, China can agree on oil price out of court – Sechin", *RIA Novosti*, 16 September 2011, available at <http://en.rian.ru/business/20110916/166896779.html>.

<sup>56</sup> Han Xiaoping, "It makes sense for China to talk away from gas deal", *China Daily European Weekly*, 28 October 2011, available at [http://www.chinadaily.com.cn/opinion/2011-10/28/content\\_13996172.htm](http://www.chinadaily.com.cn/opinion/2011-10/28/content_13996172.htm).

The Russia-China security relationship is also eroding. Russia's arms exports have collapsed from over 60 percent of total arms exports in 2005 to 6.7 percent in 2010.<sup>57</sup> The Chinese military-industrial complex now builds for itself most of what Moscow has for sale. Thus Algeria and Vietnam are now bigger customers for Russian weaponry than China. In October 2011, the FSB announced that it had arrested a Chinese spy for stealing weapons technology – a development in a relationship rarely affected by intelligence scandals.<sup>58</sup> While Russia sells equipment such as the Tupolev Tu-22M bomber to India, it refuses to sell the same equipment to China because it perceives it as a potential threat. Although the new Russian military doctrine mentions NATO 17 times and does not mention China once, Russia is in reality reinforcing its military presence in the Far East.<sup>59</sup>

China increasingly sees Russia as being in stagnation or decline and therefore as peripheral to East Asian security. Emboldened by the crisis, China feels secure enough to do without formal allies and does not want to build an anti-Western bloc. In fact, China has become increasingly assertive towards Russia. In 2008, Beijing not only declined to recognise South Ossetia and Abkhazia as expected, but also actively lobbied Russia's erstwhile allies in Central Asia to do the same. At the same time, Beijing has avoided a backlash from Moscow through strategic flattery. "We will always regard Russia as an important force," said President Hu Jintao recently.<sup>60</sup> Unlike Brussels, Beijing thus plays Russia's post-imperial neurosis to its advantage. "The Chinese are very clever," says one Russian analyst. "They treat Russia like a superpower even if they behave like it is not; they pretend that Russia is co-leader of the SCO even if it's not. This goes down well here."

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57 See SIPRI Arms Transfers Database, available at <http://www.sipri.org/databases/armstransfers>.

58 See Miriam Elder and Tania Branigan, "Russia arrests Chinese 'spy' in row over defence weapons", the *Guardian*, 5 October 2011, available at <http://www.guardian.co.uk/world/2011/oct/05/russia-arrests-chinese-translator-spying>. Previous spy scandals included the arrests of Valentin Danilov in 2001 and Evgeny Afanasiev and Sviatoslav Bobyshev in 2010.

59 "Text of Newly-Approved Russian Military Doctrine", the Office of the Russian President, 5 February 2010, available at <http://carnegieendowment.org/2010/02/05/text-of-newly-approved-russian-military-doctrine/18t>; Thomas Grove, "Analysis: Russia turns military gaze east to counter China", *Reuters*, 1 March 2011, available at <http://www.reuters.com/article/2011/03/01/us-russia-china-military-idUSTRE72027S20110301>.

60 "Chinese, Russian presidents meet for deepening strategic partnership", *Xinhua*, 17 June 2011, available at [http://news.xinhuanet.com/english2010/china/2011-06/17/c\\_13934349.htm](http://news.xinhuanet.com/english2010/china/2011-06/17/c_13934349.htm).

## An opportunity for the EU?

Putin's return could provide a short-term boost for Russia-China ties. Putin is fascinated by, and popular in, China; his daughter studied Mandarin; and his first foreign trip after announcing his return was to Beijing.<sup>61</sup> But, in the long term, mistrust between Russia and China is likely to increase. Russian and Chinese society share relatively few small- and medium-level business ties and have little human flow. Historical distrust also runs deep: whereas Western European empires exploited China and left, Russia annexed an area almost the size of Italy and France in the late nineteenth century. Although China does not make any claim to these territories, which include the cities of Khabarovsk and Vladivostok, irredentist claims are not far below the surface.<sup>62</sup>

Russian suspicions about China are metastasising into a fear that, without modernisation, the Chinese could do what many Russians accuse the West of having done in the 1990s – that is, unfairly securing Russia's juiciest economic assets. In particular, Russia fears it could lose de-facto sovereignty in its Far East. The post-crisis Russian malaise about China was captured by leading Russian expert Sergei Karaganov: "If current economic trends persist, it is very likely that Russia east of the Urals and later the whole country will turn into an appendage of China – first as a warehouse of resources, and then economically and politically. This will happen without any 'aggressive' or unfriendly actions by China. It will happen by default."<sup>63</sup>

The rise of China is thus even more problematic for Russia than it is for the West. Russia is losing its relative influence in global decision-making and could see its sphere of influence in Central Asia dissolved. This could encourage Russian leaders to reach out to Europe, as a group of leading Russian think-tankers suggested. Putin himself told an audience of mostly EU business people in October 2011 that "either we join forces or gradually leave the international arena and make room for others".<sup>64</sup>

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61 See "Putin Kicks Off Asia Trip in China", *Associated Press*, 2 December 2001, available at <http://www.themoscowtimes.com/news/article/putin-kicks-off-asia-trip-in-china/241802.html>.

62 Yuri Galenovich, "Vzglyad na Rossiю iz Kitaia," p. 272–273, Russian Academy of Social Sciences.

63 Sergey Karaganov, "Russia's Asian Strategy", *Russia in Global Affairs*, 2 July 2011, available at <http://eng.globalaffairs.ru/pubcol/Russias-Asian-Strategy-15254>.

64 Anders Aslund, "Putin Takes a Populist Turn", the *Moscow Times*, 26 October 2011, available at <http://www.themoscowtimes.com/opinion/article/putin-takes-a-populist-turn/446297.html>.

## Is Russia losing the Far East?

Russian newspapers regularly run sensationalist articles about losing the Far East to Chinese “migrant invasions”. At the root of it is the demographic imbalance between China’s Heilongjiang region which borders Russia and has a population of almost 40 million, and the Russian Far East, which has a population of only 6.5 million. In a rare moment of sincerity on China, even Putin warned a Russian town bordering China in 2000 that unless there was an improvement in the economy, their children would speak Chinese. A popular Russian joke captures this worldview: “Optimists learn English, pessimists learn Chinese and realists learn to operate a Kalashnikov.” But most credible experts estimate that there are less than 500,000 Chinese spread across Russia. There are more jobs and better prospects for migrants in south-east China than in Russia. The ageing of China’s population due to the one child policy could see an end to meaningful labour emigration by 2025.<sup>65</sup>

However, there is a real possibility that by investing more than Russia can, Moscow could “lose everything”, as Medvedev put it in 2008, compelling the government to announce some measures to modernise the region, which is underdeveloped even by Russian standards and largely dependent on trade with China.<sup>66</sup> China’s provinces are also land-hungry. In 2010, Heilongjiang province leased 4,266 km<sup>2</sup> of Russia’s territory to grow crops.<sup>67</sup> In the same year China rented another 3,450 km<sup>2</sup> of agricultural land in the region.<sup>68</sup> The Jewish autonomous oblast estimates that Chinese farmers lease 14 percent of its arable land. Chinese analysts do not deny cross-border embezzlement as a tool of influence. “This is not our responsibility, it is their problem,” says one Beijing analyst close to the Chinese Foreign Ministry. “They have an army, customs, a police force and border guards. Our businessmen are no angels. Are the Russians sleeping?”

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65 See “The Russia-China Migration and Human Capital Nexus”, Center for Strategic and International Studies, 14 April 2010, available at <http://csis.org/event/russia-china-migration-and-human-capital-nexus>.

66 “Dalniy Vostok Dolzhen Stat’ Blizhnim”, *RBK Daily*, 26 September 2008, available at <http://www.rbedaily.ru/2008/09/26/focus/382248>.

67 “Heilongjiang leases land, grows crops in Russia”, *China Daily*, 29 May 2010, available at [http://www.chinadaily.com.cn/china/2010-05/29/content\\_9907873.htm](http://www.chinadaily.com.cn/china/2010-05/29/content_9907873.htm).

68 Andrew E. Kramer, “China’s Hunger Fuels Exports in Remote Russia”, the *New York Times*, 9 June 2010, available at <http://www.nytimes.com/2010/06/10/business/global/10ruble.html>.

69 Karaganov, Bordachov and Lukyanov, “Towards an Alliance of Europe”.

At the same time, China could be a useful interlocutor for the EU in its attempts to push Russia to modernise. On certain key issues, such as corruption and the rule of law, the EU and China share goals. In fact, Chinese analysts often make similar complaints to their EU counterparts. Many of them say that the biggest problems in Chinese-Russian relations are corruption, weak rule of law, the hostile and often dangerous Russian business climate, limits on foreign investment and the frustrations of the visa regime. Thus Beijing and the EU are unexpectedly on the same page, hoping that Russia can modernise to the benefit of their own businesses. Although much will depend on the new generation of Chinese leaders who will run the country from 2012, both the EU and China would benefit from seeing Russia modernise its economy and improve its governance. The United States also shares those objectives, but it also cares less than it used to about Russia. “We have bigger fish to fry than Russia,” says one Beijing-based American diplomat.



## *Chapter 4*

# The partnership for pragmatism between the US and Russia

“We aren’t interested in a happy, friendly relationship with President Medvedev or Putin – if we get down and do substantive things, the substance would improve the relationship, not the other way around.”<sup>70</sup> This is how Michael McFaul, currently the nominee for US ambassador to Russia and one of the key architects of America’s new Russia policy, explains the main logic behind the principal change in US-Russia relations. As a result, the relationship between Moscow and Washington has been given a boost. Thanks to America’s “reset” and Russia’s newfound interest in co-operation with the West, Russia-US relations are the best they have been in a decade – and in some ways are more productive than Moscow’s relations with the EU.

Four years ago, when the EU was deeply divided about whether to contain or engage Russia, US relations with Moscow had hit rock bottom. The eight years of President Bush and President Putin saw the relationship sour from an incipient strategic partnership in a “global war on terrorism” to outright animosity. Washington worried about the Kremlin’s ambitions to reassert its dominance in the CIS or Russia’s tacit support for Iran’s nuclear programme. Moscow, on the other hand, saw the US as a direct sponsor of anti-Russian “colour revolutions” and an unwelcomed intruder in its post-Soviet backyard. The war in Georgia brought the relationship to a post-Cold War low. Yet despite all these problems, President Bush’s successor has relatively quickly managed to turn the corner with Moscow.

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<sup>70</sup> Remarks by Michael A. McFaul, “Russia after the Global Economic Crisis”, Peterson Institute for International Economics, 10 June 2010, available at [http://www.piie.com/events/event\\_detail.cfm?EventID=154&Media](http://www.piie.com/events/event_detail.cfm?EventID=154&Media).

## A transactional relationship

When he became president in 2009, Barack Obama inherited a country struck by the worst economic crisis since the Great Depression and overstretched abroad. His foreign-policy priorities differed from that of his predecessor: his top two goals were to prevent the spread of nuclear arms (particularly to Iran) and to win the war in Afghanistan. Believing that the US had lost the moral high ground to champion any particular set of values, Obama remained cool to democracy promotion and NATO enlargement eastward. With the US increasingly focused on Asia, Russia has dropped down its list of priorities. For example, a recent article by Secretary of State Hillary Clinton about “America’s Pacific century” does not mention it once.<sup>71</sup> This shift has almost inadvertently created a basis for improvement in relations with Russia: the US sought Russian co-operation on Iran, Afghanistan and nuclear arms reductions, and de-emphasised – though did not scrap – divisive issues such as NATO expansion or democratisation.

In less than two years, this new transactional approach has produced a less toxic atmosphere between Washington and Moscow, and has delivered concrete, if limited, progress in areas in which the US had previously struggled. More than 100,000 NATO troops have crossed Russia’s territory en route to Afghanistan and around 40 percent of all Afghanistan-bound supplies now pass through Russia, avoiding the ambush-prone logistics line through Pakistan. The US also got Moscow to change its relationship with Iran: besides supporting a new round of sanctions at the UN Security Council, it also relinquished an \$800 million contract for an S-300 air defence system to Tehran, even though the sale would not violate the international sanctions regime. Russia has also shut down its last remaining weapons-grade plutonium production reactor and ratified the 123 Agreement opening new avenues for co-operation on civilian use of nuclear energy. The new START treaty ratified by both Washington and Moscow earlier this year also brought progress by removing almost a third of strategic nuclear weapons on the US and Russian side (although the deal has also made it clear that Russia is not keen to go further in reductions). Thus the “reset” has delivered better and safer access to Afghanistan, a more united international

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<sup>71</sup> Hillary Clinton, “America’s Pacific Century”, *Foreign Policy*, November 2011, available at [http://www.foreignpolicy.com/articles/2011/10/11/americas\\_pacific\\_century](http://www.foreignpolicy.com/articles/2011/10/11/americas_pacific_century).

<sup>72</sup> “Sergei Magnitsky: Russia angry over US visa ban”, BBC News, 28 July 2011, available at <http://www.bbc.co.uk/news/world-europe-14323398>; “Preliminary conclusion of the working group on the study of circumstances of Sergei Magnitsky’s death, the working group on civic engagement in judicial reform, the working group on citizen participation in prevention of corruption and public safety”, July 2011, available at <http://russian-untouchables.com/rus/docs/Civil-Right-Council-conclusion-report-Executive-summary-ENG.pdf>.

## The Magnitsky case

Sergei Magnitsky was a Russian lawyer working for Firestone Duncan, a law firm that represented the London-registered investment company Hermitage Capital Management in a case of alleged tax evasion and tax fraud in Russia. Hermitage started to run into problems in 2006 after it provided details to the press on misconduct and corruption in a number of Russian state-owned companies.

In 2007, a group of Ministry of Interior officers raided the Moscow offices of Hermitage Capital and Firestone Duncan and seized company documents. Soon afterwards, Viktor Markelov, a Russian citizen who had previously been convicted for murder, claimed ownership of three fully-owned Hermitage subsidiaries. These subsidiaries were then sued by an unknown company, ZAO Logos Plus, for an outstanding debt. At a court hearing, lawyers claiming to represent Hermitage agreed to pay damages totalling nearly \$1 billion. Afterwards, arguing that the damages meant the company had made a loss in the previous year due to these unpaid debts, Markelov filed for a tax rebate of \$230 million, which was granted in a matter of days.

In his subsequent testimony in court, Magnitsky claimed that the seized documents were used to re-register the ownership of Hermitage's subsidiaries and he accused the police, tax officials and the judiciary of sanctioning a wide-scale tax fraud. In November 2008 he was arrested and imprisoned in Moscow without trial and denied medical care. He died in a cell in November 2009. An investigation by President Medvedev's Human Rights Council in July 2011 concluded that there was a reasonable suspicion that Magnitsky's death was triggered by beatings while in police custody.<sup>72</sup>

Congress passed the Justice for Sergei Magnitsky Act in 2011, banning around 60 Russian officials allegedly implicated in the scandal from entering the US and freezing assets held in the US. In July the State Department placed similar visa restrictions on unnamed Russian officials. This prompted the Russian Ministry of Foreign Affairs to start working on a similar list of Americans said to have violated the rights of Russian citizens, such as the arms dealer Viktor Bout, who is currently in US custody.

action on Iran and concrete steps towards nuclear arms reduction. As Sam Greene, an American expert, puts it: “The US got what it wanted – Russia is no longer a problem.”

Washington achieved all of this without changing its mind about Russia: the US leadership continues to think poorly of its Moscow counterparts and Russia’s economic and political prospects, and has not completely stopped criticism of human rights abuses inside Russia. Obama administration officials continue to push for investigations into the murders of Russian journalists and Congress has banned Russian officials deemed to be involved in the death of lawyer Sergei Magnitsky (see box) from entering the US. USAID funds for civil society in post-Soviet space including Russia have in fact increased. Thus the key to Washington’s success with Russia was not a drastic change of mind about Russia, but its ability to compartmentalise its relations with Moscow to a point where disagreements on particular issues don’t poison the overall relationship.

The “reset” is also seen as a qualified success in Russia, albeit for entirely different reasons. Moscow has interpreted the fact that the Obama administration has toned down rhetoric about NATO’s eastward expansion and democracy promotion as a “de facto recognition of Russia’s special interests in the former Soviet Union”, as Sergei Karaganov puts it.<sup>73</sup> A Russian lawmaker concurs with this assessment: “We had to respond when the US wanted to grab Georgia to NATO, but we now must build rational relations with the United States.” The economic crisis in the US has also persuaded Russia that American decline is slow but inevitable – much to Moscow’s delight.<sup>74</sup>

In Russia’s view, this “rational relationship” with the US has brought some benefits: in return for Russia’s accommodation of some of the American demands, the US allowed Russia to consolidate its influence in its “near abroad” and no longer pokes its nose into Ukraine or Georgia. For example, a prominent Russian politician believes that “in 2010, the US finally allowed the Ukrainians to choose their president”. These comments illustrate the level of paranoia that existed during the Bush era about the US being a competitor in Russia’s own backyard. But whether or not this perception was justified, the comments also show that Russia is no longer as obsessed about the US as it used to be.

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<sup>73</sup> Sergei Karaganov, “After the “reset””, *Russia in Global Affairs*, 26 October 2010, available at <http://eng.globalaffairs.ru/pubcol/After-the-“reset”-15027>.

<sup>74</sup> “The US-Russia Relations after the ‘Reset’: Building a New Agenda. A View from Russia”, Valdai Discussion Club, March 2011, available at <https://files.me.com/karaganovsergey/gfjyws>.

By allowing the transit of Afghanistan-bound troops and supplies, Russia has also helped itself: without NATO's presence, extremism and terrorism would soon spill over to the neighbouring Central Asian republics and directly affect Russia's own southern border. Russians are the first to acknowledge this and realise that they need NATO in Central Asia: "otherwise", says an analyst close to the Kremlin, "we lose". In the past, Russia openly lobbied Kyrgyzstan's government to evict the US from their military base in Manas. Now things are different: Washington and Moscow closely co-ordinated their response to the chaos triggered by the ouster of President Bakiyev in spring 2010 and to the subsequent ethnic clashes in southern Kyrgyzstan.

However, de-emphasising the issue of Russia's less-than-ideal state of democracy and worsening human rights record has cost the US some of its soft power inside Russia. An expert close to United Russia pointed out that such US behaviour strengthened a perception of American "hypocrisy". This further reinforced the feeling among many Russians that Washington brings up issues such as human rights and democracy not because it believed in such values but in order to put pressure on Russia.

## The limits of the "reset"

Although it has been something of a success, the new transactional relationship between the US and Russia has its limits. Security policy – the area in which there has been most progress since the "reset" – has now turned into the greatest obstacle to continued good relations between Washington and Moscow. Russia was initially pleased with Obama's decision to scrap Bush-era plans for a missile-defence shield in Europe that included a radar station in the Czech Republic and long-range missiles deployed in Poland. But the administration's new plan for a "European Phased Adaptive Approach" would see American cruisers off the coast of Europe and the deployment of interceptors of short-range missiles (and after 2020 of long-range missiles) in Poland and Romania. A few days after the NATO-Russia summit in November 2010, President Medvedev warned of the danger of a "new arms race" and suggested that Russia might have to respond to the new US plans by deploying new strike equipment.<sup>75</sup>

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<sup>75</sup> "Medvedev sees arms race if missile shield not agreed", BBC News, 30 November 2010, available at <http://www.bbc.co.uk/news/world-europe-11872801>.

## The US-Russia Bilateral Presidential Commission

The Bilateral Presidential Commission (BPC) set up by Obama and Medvedev has wider scope and more flexibility than similar efforts in the 1990s such as the Gore-Chernomyrdin Commission and the 2000s during the presidencies of Bush and Putin. The BPC consists of a steering group co-chaired by US Deputy Secretary of State William Burns and Russian Deputy Foreign Minister Sergey Ryabkov. It has 21 substantive bilateral working groups whose chairpersons and co-ordinators are usually at the level of deputy minister/deputy secretary of their respective agency (such as US Secretary of Defence Leon Panetta, Russian Defence Minister Anatoliy Serdyukov and First Deputy Chief of Staff of the Russian Presidential Administration Vladislav Surkov).

The co-ordinators have been enjoined to avoid “big show” meetings. Instead, small working groups include participants from various agencies on both sides and use videoconferencing as much as traditional meetings to move from policy conception to project reality. The working groups on security issues have made the most progress (for example, by getting Russia’s support for multilateral sanctions on Iran) but there have also been agreements to begin and enhance co-operation on scientific research (especially in clean energy, public health and basic science). Although much of the work of the BPC still consists of meetings and signing agreements at the working level, the extent and depth of the bilateral consultations between the two countries is unprecedented.

The “reset” between Moscow and Washington created a thicker political relationship between the two countries – the US-Russia Bilateral Presidential Commission set up by Obama and Medvedev (see box) comprises 21 working groups whose members deal with issues ranging from arms control to energy efficiency to civil society. But it has yet to yield major economic benefits. The trade relationship between the two countries remains limited. Although Russia is the world’s sixth-largest economy by purchasing power parity, the US trades less with it than with Singapore or Ireland.<sup>76</sup> While Washington supported

Russia's entry into the WTO, Moscow's membership in the organisation is not expected to be a game-changer in US-Russia trade relations. US diplomats in Moscow now quote Germany's robust trade relations with Russia as an example of success to which they aspire.

In other areas, the US-Russia "reset" has not worked at all. Russia has not become more co-operative on other pressing international issues such as Syria and it continues its military co-operation with Venezuela, to the annoyance of Washington. Although Moscow did not veto the UN resolution on Libya, it has since then launched a war of words on the Western role in the Arab spring. US officials themselves admit that while the "reset" has been a success on a number of issues, the chances for further headway are limited. "Frankly, we don't expect anything from Russia", replied a State Department official when asked about the future. As the American presidential election approaches, the "reset" policy – and Obama specifically – is likely to come under attack for selling out on Russia's human rights.

## Leaving from behind

The US-Russia "reset" has both admirers and critics in Europe. Some European experts and officials see it as Obama's biggest foreign-policy success, while others argue that it has brought little substance beyond an improved atmosphere between the two capitals. Others still insist that the "virus of the 'reset' must be stopped". However, such criticism misses a more fundamental change in America's attitude towards Russia, which is likely to persist: the long-term shift in US foreign policy away from the Atlantic and towards the Pacific that simply makes Russia a lower priority for Washington than it has been in the past. But while the US can afford to de-prioritise Eastern Europe, Russia and the South Caucasus, the EU cannot. As a direct neighbour of Russia, its relationship with Moscow – which is much more complex than that of the US – is likely to remain a higher priority for Europeans.

So far, EU member states have indirectly benefitted from the improved relations between America and Russia: Obama's policy dovetailed with Poland's rapprochement with Russia, and the EU's own efforts on Iran were boosted by Russia's more co-operative stance. The "reset" was also an impetus for the EU member states to rethink their own relationship with Russia. "We don't want to argue with Russia any more", says a Central European diplomat in Moscow. A diplomat from a Baltic state agrees: "Our relations have never been

as good as now – they are calmer and civilised, also thanks to the ‘reset’.” All of this has helped forge a new EU consensus on engagement with – rather than containment of – Russia, bringing the views of previously sceptical eastern member states and the likes of Germany or France closer to each other.

However, the EU has yet to come up with a coherent strategy that will fill the vacuum that is increasingly being created by the US’s relative de-prioritisation of Russia, Eastern Europe and the South Caucasus. There has been much discussion of the new US strategy of “leading from behind”. But, in the case of Russia, it is more likely to “leave from behind”. This means that the EU’s role will be more important in the region than ever before. But just as the US has soured on NATO expansion, the EU has lost its appetite for further enlargement. The changing nature of the US relationship with Europe means that the EU is now on its own in its eastern neighbourhood. While the US will remain politically, militarily and economically engaged in Europe, it is the EU that now needs to take the lead in making wider Europe both more democratic and secure.



## Chapter 5

# The underperforming EU

Just as Russia's illusions about being a BRIC have been shattered, so have the EU's dreams of being a "normative superpower". Elites across the European continent face a crisis of confidence shaped by financial volatility, changing demographics and a power transition towards Asia. As both the EU and Russia have focused on the domestic consequences of economic turmoil, the relationship between them has become less fraught. But paradoxically the EU seems to have treated Russia more – not less – like a BRIC since 2008. For most of the 1990s, Europe hoped it could transform Russia into a "big Poland" that it could influence through conditionality. The EU has now given up on that transformative project and seems reconciled to accepting Russia as a "small China" with which it does business but does not criticise or try to change.

The euro crisis has pushed some member states to the brink of default, undermined solidarity among member states and damaged the EU's prestige. However, despite the crisis, there have been two important developments during the last few years that could give it greater leverage over Russia than it had in the past. The first is that the EU has taken steps to reduce its energy vulnerability towards Russia. The second is that member states, which were deeply divided over Russia, have converged in their views of, and approaches to, Russia. There is now a consensus that Russia is a partner with which the EU needs to engage rather than an adversary that needs to be contained.

### Towards greater convergence

In 2007, when ECFR published its *Power Audit of EU-Russia Relations*, Russia was the EU's most divisive foreign-policy issue. The relationship between the EU and Russia was characterised by "asymmetric interdependence": Russia was able to turn its relative weakness into power by exploiting internal divisions

within the EU, which turned the EU's power into weakness. Russia pursued bilateral energy deals with some member states, while engaging in various diplomatic, trade or security disputes with others, using everything from oil supply cuts to trade embargoes. The EU was divided between member states such as Germany or Italy that wanted to engage Russia almost at any cost and others such as Poland and Lithuania that wanted to contain Russia. This prevented the development of common EU approaches to Russia. Press articles looked like dispatches from a diplomatic battlefield. Germans saw Poland and Lithuania as unconstructive and Poles saw Germany as a Russian "Trojan horse" within the EU.<sup>77</sup>

In the four years since then the various EU member states have moved from the two extremes of engagement and containment towards the centre ground. The implicit deal is that large member states such as Germany and France will show more solidarity with new member states facing trouble with Russia, which will in turn be less disruptive of co-operation with Russia on trade or a new comprehensive EU-Russia agreement. As a result, there are no "new cold warriors" left. For example, Lithuania's own diplomats say that "for the first time in years there is nothing dramatic in our relations with Russia – neither big progress nor a big crisis". Above all, there has been a degree of convergence between Germany and Poland – the two countries that are most important in defining EU-Russia policy. Just how much things have changed was illustrated by the joint letter from the German and Polish foreign ministers in November calling for a joint EU approach to Russia "based on shared interests and objectives".<sup>78</sup>

This relative convergence has been made possible by movement on both sides. On the one hand, Germany, arguably Russia's best friend in the EU, has become more hard-nosed: although its overriding desire is to engage with Russia, it sent a clear signal to Moscow that EU-Russia relations are unlikely to progress unless Russia normalises relations with countries such as Poland.<sup>79</sup> On Berlin's initiative, the EU made the establishment of a Joint Political and Security Committee with Russia – which could give greater access to intra-EU foreign-

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77 Andrew Rettman, "Polish FM in Wikileaks: Germany is Russia's Trojan horse", *EU Observer*, 16 September 2011, available at <http://euobserver.com/24/113652>.

78 Joint letter of Foreign Ministers Radoslaw Sikorski and Guido Westerwelle of Germany on EU-Russia relations, 17 November 2011, available at <http://www.ms.gov.pl/index.php?document=46717>.

79 Andrew Rettman, "Poland triumphant after icy EU-Russia summit", *EU Observer*, 21 May 2007, available at <http://euobserver.com/24/24094>.

policy discussions – conditional on Moscow’s active co-operation on resolving the Transnistria conflict. Germany has also emerged as one of the toughest negotiators in talks on Russia’s WTO accession.<sup>80</sup> Berlin has become even more sceptical about Russia since the announcement of Putin’s candidacy for the 2012 presidential election, which has undermined its hopes for modernisation.

On the other hand, Poland has “normalised” its once-fraught relations with Moscow. Even though Russia held military drills simulating a nuclear attack against Poland in 2009, relations have drastically improved, culminating in the symbolic embrace between Putin and his Polish counterpart Donald Tusk at the site of the plane crash in Smolensk that killed the Polish president and 95 others in April 2010. Poland’s abandonment of its “soft containment” strategy effectively unblocked EU-Russia relations on a number of fronts. As Eugeniusz Smolar, a Polish expert, puts it: “We are not going to be on the barricades every time Russia misbehaves.” What another specialist calls a “cold peace” has in turn allowed Warsaw to patch up relations with Berlin. The German-Polish rapprochement led to the establishment of a regular high-level dialogue between Warsaw, Berlin and Moscow and a visit by the German and Polish foreign ministers to Belarus in the run-up to the December 2010 presidential election. On such joint actions, as Smolar puts it, “Germany provides the muscle and Poland the credibility”.

While overcoming its internal divisions, the EU has also started to take steps to reduce its dependence on Russian energy. Before 2008, member states scrambled to secure long-term deals with Gazprom. But, as the economic crisis kicked in, the EU’s gas consumption fell and companies from several states, including Italy, Germany and the Netherlands, forced Gazprom to either concede to a reduction of prices or face arbitration. At the same time, alternatives to pipelined gas from Russia such as liquefied natural gas (LNG) and shale gas have emerged. In particular, the US shale-gas market boom freed up LNG to be redirected from the US to the EU, which has managed to build more LNG terminals. In the medium term, the drilling of shale-gas reserves in Poland and some other Central European countries could release enough gas to moderate

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**80** Apart from Georgia’s demands to have access to information about trade in South Ossetia and Abkhazia, the talks on Russia’s WTO entry were held up due to an eight-year import tax break that Moscow had afforded for car manufacturers in exchange for producing 300,000 cars annually. The EU, led by Germany, said this violated WTO agreements (the provision heavily affected Germany’s own carmakers). Berlin openly complained about Moscow’s protectionism, whereas most other EU member states seemed to be more flexible on Russian demands. See Gleb Bryanski, “Russia’s 2011 WTO entry hinges on EU: Kremlin”, Reuters, 15 September 2011, available at <http://www.reuters.com/article/2011/09/15/us-russia-summit-wto-idUSTRE78D44E20110915>.

potential hikes in European gas prices, minimise the monopoly premium paid for Russian gas and potentially minimise the dependence of several EU member states on gas delivered from Russia. “In the long run, this could have disastrous implications for Russia’s gas exports,” says one energy analyst.

Since the 2009 Russian-Ukrainian gas spat, the EU has accelerated attempts to revamp energy infrastructure to help avoid or better deal with potential cut-offs. A quiet revolution is now underway as member states, including those highly dependent on Russian gas, are rebuilding or adding infrastructure to make flows in their cross-border gas pipelines reversible and build interconnectors linking gas systems with that of other member states. By the end of 2011 a reverse flow of gas should be possible between Poland and Germany; Slovakia would be linked to Austria’s energy hub; and capacities of gas storage at the Czech-Polish border will be substantially increased.

The EU has also made progress in liberalising its energy market and thus started sapping Gazprom’s monopolies. The “third energy package” requires EU member states either to force energy companies to fully unbundle their gas operations or to retain ownership but ensure activities in gas transmission are separated from those of production. These new EU rules exempt the recently completed Nord Stream gas-transit project but South Stream – another of Russia’s pet gas-transit projects – is likely to be affected. They have helped turn the EU’s dependence on Russian gas into potential leverage: Russia has now become the *demandeur* pleading for exemptions or the non-implementation of the package towards its investments. In a 2011 outburst in Brussels, Putin accused the EU of “confiscation of property”.<sup>81</sup> In future, the European Commission may have an even greater say over the gas-supply deals between member states and third countries, and strike down bilateral deals that contravene EU law and be able to represent the EU in talks with third countries.<sup>82</sup> Gazprom’s operations in the neighbourhood may also suffer: both Moldova and Ukraine have agreed to join the EU-led Energy Community and will implement the third energy package by 2015. Russia has put them under increasing pressure to renege on their commitment.<sup>83</sup>

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**81** Stephen Castle, “Putin Questions Europe’s Foreign and Energy Policies”, the *New York Times*, 24 February 2011, available at <http://www.nytimes.com/2011/02/25/world/europe/25putin.html>.

**82** “Communication on security of energy supply and international cooperation – The EU Energy Policy: Engaging with Partners beyond Our Borders”, European Commission, 7 September 2011, available at [http://ec.europa.eu/energy/international/security\\_of\\_supply/cooperation\\_en.htm](http://ec.europa.eu/energy/international/security_of_supply/cooperation_en.htm).

**83** “R. Moldova va putea primi gaz european: În 2012 va începe constructia gazoductului Ungheni-Iasi”, *Unimedia*, 6 October 2011, available at <http://unimedia.md/?mod=news&id=39810>.

Russian gas remains of huge importance for the EU: more than a third of EU gas imports come from Russia.<sup>84</sup> In fact, Germany's decision to phase out nuclear power by 2020 will likely result in increased gas demand, which will make it more dependent on Russia, at least in the medium term. But German gas markets are crucial for Russian energy companies and Moscow would never bully Berlin as it used to with Lithuania or Poland. Meanwhile, thanks to the measures agreed between member states, some of the vulnerable countries such as Lithuania, Bulgaria or Slovakia, which have all suffered from past gas-supply disruptions, could soon be better protected from cut-offs than they were a few years ago.

## United in underachievement

Yet despite this newfound consensus and diminished vulnerability, the EU is underperforming in its relationship with Russia. Perhaps the best example of this is the Partnership for Modernisation, launched with great fanfare in June 2010, which aims to help the EU modernise Russia's economy and its political institutions. The initiative was a product of Germany's desire to help Russia modernise through greater interdependence and the EU's attempt to strengthen Medvedev and turn his rhetoric of "modernisation" into concrete outcomes such as expanding investment, boosting trade, improving energy efficiency, as well as fighting corruption and promoting the rule of law and people-to-people links.<sup>85</sup>

However, the EU and Russia want different things from this initiative. For Russia, "modernisation" is primarily a matter of importing Western technology, know-how and investments. At the outset of the project, the EU, on the other hand, viewed it as a vehicle through which it could smuggle in institutional and political modernisation by arguing that one cannot modernise simply by importing machinery if there is no rule of law and corruption is rife. This is fine in theory. But the EU's ability to leverage its potential political influence depends on its ability to act in unison and its willingness to push for political change. So far, it has failed in both respects.

In particular, the success of the EU's Partnership for Modernisation has been undermined by the separate bilateral partnerships that 18 of the EU's 27

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<sup>84</sup> For more information on EU-Russia energy relations see [http://ec.europa.eu/energy/international/russia/russia\\_en.htm](http://ec.europa.eu/energy/international/russia/russia_en.htm).

<sup>85</sup> Joint Statement on the Partnership for Modernisation, Council of the European Union, EU-Russia Summit, 31 May–1 June, available at [http://www.consilium.europa.eu/uedocs/cms\\_data/docs/pressdata/en/er/114747.pdf](http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/er/114747.pdf).

member states have with Russia. Member states do not normally co-ordinate these partnerships or even inform each other properly of what they contain. As a result, they have quickly turned into little more than an instrument for member states to promote their own business interests. Meanwhile, for Russia they are a good way to acquire technological know-how without pursuing political and institutional modernisation. One EU diplomat in Moscow described his country's bilateral partnership as follows: "We have no political issues, only economic ones. We see the partnership as a way to clear the way for our companies into Russia." In short, the EU has not used its collective weight to push harder to achieve an improvement in the rule of law or reduce corruption.

Another example of the EU's failure to capitalise on Russia's post-BRIC weakness is visa liberalisation – the single most substantial and visible issue on the EU-Russia bilateral agenda. In 2007, Moscow and Brussels started talks about possible liberalisation of their visa regime that could eventually lead to visa-free travel. In late 2011, Russia and the EU agreed on a set of common steps towards full liberalisation of the visa regime. Yet member states differ on how fast the EU should move towards visa-free travel.

For the Russian elite, access to the EU is a source of security: much of their property is in the Côte d'Azur; their savings are in Luxembourg; and their children study in the UK. Should the weather turn sour for a Russian businessman or politician, the EU is the eventual escape. "Visas are the ultimate source of leverage that Europe has over the Russian elite: the moment anything goes wrong they all want to be at the airport and able to flee in minutes," says one Russian commentator. A visa-free regime with the EU is therefore the one thing Russia wants most of all. For the EU, on the other hand, the issue of visa liberalisation touches sensitive nerves related to domestic debates on immigration.

However, because EU member states take very different approaches to the issue, they are unable to use Russia's desire for visa liberalisation as leverage. Although the Schengen area has a common visa policy, real-life visa-issuance practices still remain quite divergent. While some Schengen countries such as Belgium, Germany and the Netherlands worry about immigration and therefore apply more restrictive visa policies, others such as Spain, Italy and Greece are keen to encourage tourists and are therefore much more flexible. Finland is the most liberal of all: its consulate in St Petersburg issues 700,000 visas a year. These different approaches encourage "visa shopping" by Russian citizens, which undermines the EU's leverage.

While the EU has agreed on a set of conditions that Russia should meet to get the visa-free regime, there is no agreement on how to assess whether or not they are fulfilled on the ground. The EU also disagrees as to whether or not a visa-free regime should follow automatically upon Moscow meeting the criteria. Some member states think the EU should set the bar high, as it did in the Western Balkans, and make Moscow sweat in order to get an offer of a visa-free regime, with meticulous monitoring in place. It could, for example, demand not just an improvement of border management and better security of documents (including biometric passports), but also deeper reforms of the law-enforcement agencies and real progress in tackling corruption and improvements in human rights. Some major EU players even consider linking a visa-free regime to political concessions by Russia – for example, a more constructive role on conflict settlement in Moldova.

In times of crisis, EU politicians have little to gain from arguing for a fast-track approach towards Russia. Many fear that a relatively quick visa liberalisation could lead to problems for Europe – particularly in terms of criminality and immigration. “Russia is too big,” a diplomat from an EU member state says. “You can take a chance with a visa-free regime for Macedonia, but not with Russia.” Another Baltic state diplomat adds: “It is easy for Spaniards to push for visa-free with Russia. They will get the rich oligarchs on the Spanish coast and we will get the petty criminals.” There are also legitimate concerns about the influx of migrants who can legitimately claim asylum due to repression in the North Caucasus or elsewhere.

The problem with a more thorough approach is that conditionality has worked towards Serbia and might work in Moldova but is unlikely to work with Russia. Russia is much bigger and therefore allergic to unilateral imposition of EU conditionality. In addition, Russian elites have few problems getting Schengen visas and holders of diplomatic passports travel visa-free, while public pressure to deliver on necessary reforms to achieve visa-free status with the EU is smaller. They therefore have few incentives to change the way that Russia is governed (which could undermine their positions) for the sake of the ability of an average Russian citizen to travel without a visa. What the EU needs in the short term is a middle way that reconciles the visa-free sceptics with the visa-free liberals. Such a system would make life easier for legal travellers from Russia, while maintaining a strong-enough monitoring mechanism that would allow the EU to deny access to unwanted visitors.

## A more proactive approach

The lack of real progress on the Partnership for Modernisation and visa liberalisation is symptomatic of a broader failure of the EU's foreign policy towards Russia. Although the EU is more united than it was a few years ago, it still does not have a co-ordinated approach towards Russia and is not pushing Russia to modernise hard enough. "It's not enough to speak with one voice," says one senior EU diplomat. "We also need to say something meaningful." Now that Putin is returning to the presidency, the EU will have to turn its soft consensus into a more proactive stance that is predicated on realism rather than wishful thinking about Medvedev's ability to modernise Russia.

However, as it struggles to solve the euro crisis, the EU now faces the prospect of the emergence of a two-speed Europe, which would have huge implications for the possibility of such a coherent foreign policy. In particular, as David Miliband has argued, a two-speed Europe would be unbalanced in its policy towards Russia.<sup>86</sup> Russian strategists are themselves aware of this. As one Russian expert notes: "Talk of multi-speed Europe worries Russian financiers, but gives a lot of pleasure to Russian diplomats who hope to fish for friends in a weaker and more divided Europe."



## *Chapter 6*

# An EU strategy for a post-BRIC Russia

The euro crisis is already having serious foreign-policy implications for the EU: its economic power is being questioned and its “soft power” shattered, and there is a risk of spill-over from a multi-speed EU on economic issues into foreign-policy disunity. This makes it harder, but also more important, for member states to find ways to develop a more effective foreign policy in order to avoid greater fragmentation of the EU. In particular, Russia remains a hugely important foreign-policy issue for the EU. But although Russia has lost much of its pre-crisis self-confidence, streamlined its ambitions in the post-Soviet space, feels threatened by China and has “reset” relations with the US, the EU has yet to develop a strategy for dealing with a post-BRIC Russia.

If it overcomes the euro crisis, the EU could be in a better position than during Putin’s first two terms as president to achieve a more effective approach towards Russia. Member states have united around a new consensus as Germany has become more hard-nosed and Poland has “normalised” its relations with Russia. Yet despite this, the EU has not achieved more: it has kept its focus on macro-objectives rather than the kind of concrete deliverables that lie at the heart of the success of the US-Russia “reset”. In order to exploit the opportunities created by Russia’s post-BRIC predicament – but also to protect itself against the possible threat of a stagnant but nationalist Russia – the EU should adopt a strategy centred around further strengthening its unity and deepening engagement with Russia while limiting Putin’s room for manoeuvre to manipulate asymmetric interdependence with the EU.

## A stronger EU

The EU has a strong interest in developing its partnership with Russia. A modernising Russia will unlock growth potential for the country itself and will be in the EU's economic, political and security interests. But without the EU leveraging its unity and collective weight, it will not achieve its objectives on Russia. The German-Polish motor is a credible vehicle through which that can be achieved by bringing together two states that have different perspectives on Moscow, but also have a deep interest in a proactive EU policy on Russia. In particular, the EU should:

- **co-ordinate bilateral Partnerships for Modernisation.** There is currently little common ground between member states on what Partnerships for Modernisation should involve. Greater co-ordination and agreement on key rule of law priorities could leverage the Europeans' greatest asset towards Russia: their unity. To achieve this, representatives of the European Commission and the European External Action Service (EEAS) should be invited to take part as observers in the bilateral Partnerships for Modernisation between Russia and member states. The accession of Russia to the Organisation for Economic Cooperation and Development (OECD) – which would help increase transparency and improve governance and corporate practices and assist Russia to meet the requirements set out in the OECD accession roadmap – should therefore be one of the key priorities for the bilateral partnerships for modernisation. To improve coordination, the EEAS and member states should report annually on progress on their partnerships and share and discuss reports in Brussels committees such as COEST (EU Working Party on Eastern Europe and Central Asia) and EU and national embassies in Moscow. Member states should be required by the EU to have far greater transparency and information-sharing on financial, technical and practical details of their projects in order to avoid duplication.
- **pass a European anti-corruption law.** As well as pushing harder on the rule of law as part of its Partnerships for Modernisation, EU member states should pass anti-corruption legislation modelled on the UK's recent Bribery Act 2010. This bans companies which operate in the UK from being engaged in corrupt practices both in the UK and elsewhere in the world – including Russia – and opens up the possibility for their prosecution in the UK. Legislation of this kind could contain the spread of corrupt practices in the dealing of EU companies in Russia and would serve the declared objectives of the Partnership for Modernisation. The EU should also support anti-corruption activists within Russia.

- **launch an EU Business-to-Diplomats Taskforce.** The EU's objectives are not just disconnected on a national level but also on a sectoral level. European business and foreign-policy goals are often at odds and undermine each other. An EU taskforce bringing together respective stakeholders on Russia policy from these two fields could be a way to begin a dialogue about how to achieve less lopsided results and work on a common co-ordination platform. This should not just be a lobbying platform for businesses but also a way for decision-makers to co-ordinate their political objectives with business interests.
- **support EU companies to renegotiate gas-price formulas with Gazprom.** Gazprom is now being taken to arbitration by many of its EU partners such as E.ON and RWE, which are hoping to force a change to gas-pricing formulas which are currently based on the price of oil. In this strategically important and highly politicised business, EU member states should support the change in gas-pricing formulas for EU customers in a way that reflects closely the existing supply of gas through LNG terminals or shale-gas developments, not oil price volatility.

## Engaging Russia

A stronger EU should also more actively engage Russia on issues of primary importance. The EU could spearhead engagement with Moscow on a number of issues such as improving the conditions of travel for Russian citizens into the EU and strengthening foreign-policy engagement. To achieve these aims, the EU should:

- **adopt an electronic visa system with Russia.** The EU-Russia visa-free regime is likely to become a reality in the medium-to-long term. The EU and Russia should do their utmost to move as fast as possible towards a visa-free regime. But even before then, EU visa policies could be drastically improved through the adoption of an electronic visa system with Russia, which the EU should also put on the table for Moldova, Ukraine and other eligible EaP countries. Under such a system, inspired by the Mexican visa model for a number of countries including Russia, all Russian citizens who have been granted at least one conventional Schengen visa could apply for their subsequent trip to the EU online without having to go to an embassy or consulate. Unless they are rejected within seven or 14 days, the applicants should be allowed to travel to the EU using a print-at-home e-visa with a barcode containing relevant information. Such a system would drastically facilitate travel for bona fide travellers, while

allowing EU member states to maintain a high degree of security of their borders and ability to filter travelling and migration flow. This kind of visa system is now possible thanks to the centralised input into the Visa Information System, the Schengen area's database, which has been recently significantly upgraded. It would also send a clear signal to Russians that they are welcome in the EU and would give a boost to the EU's efforts to build more links with the Russian society. In return, the EU should demand significant visa facilitation on the Russian side.

- **co-ordinate on visas.** Although the EU stands for the rule of law, several EU member states adopt highly restrictive visa policies which often disregard the EU-Russia visa facilitation agreement (VFA) when it comes to granting long-term and multi-entry visas. The European Commission should initiate annual monitoring reports on EU member states' compliance with the VFA and use peer pressure to improve visa-issuance practices. The EU's model of verifying compliance by member states of Schengen rules through on-site visits and monitoring could be gradually used to verify compliance with EU visa-facilitation agreements as well.<sup>87</sup> A "complaints hotline" for visa applicants from the countries with a VFA (including Russia) could also be developed to feed into the monitoring work.

The EU should also engage Moscow more on regional security issues. Now that Russia is less obsessed by NATO and more concerned by Central Asia than it used to be, the EU and Russia could develop a strategic dialogue on security issues outside Europe and in the common neighbourhood. The EU could therefore:

- **create an EU-US-Russia partnership in Central Asia.** Moscow is nervous that a post-American Afghanistan and state fragility in Kyrgyzstan and Tajikistan could threaten Russia. New insurgencies or state collapse could export uncontrolled mass migration, drugs and even insurgents themselves into Russia as well as the EU. With NATO readying to stop combat operations in Afghanistan by the end of 2014, the EU should, together with the US, launch a systematic strategic dialogue on bolstering Central Asia's security. The EU's added value could be in developing a partnership on soft-security issues and possibly a joint EU-Russia border assistance mission to strengthen border security in Tajikistan and Kyrgyzstan.

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<sup>87</sup> "Schengen governance – strengthening the area without internal border control", European Commission communication, 16 September 2011, available at <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=COM:2011:0561:FIN:EN:PDF>.

- **develop co-operation with the CSTO and the Shanghai Cooperation Organisation.** The EU should learn from the US and China, which have deployed strategic flattery to improve their relationships with Russia. The EU should begin a structured dialogue with both organisations about the regional challenges and ways to maintain stability once NATO withdraws from Afghanistan.
- **strike a grand bargain on EU-Ukraine free trade.** Instead of playing a zero-sum game in Ukraine, the EU should try to help Kyiv escape the “either/or” choice between deep free-trade with the EU or the Russian-led Customs Union. One possible way out would be to offer Russia a deal on an EU Free Trade Area with the Russia-Belarus-Kazakhstan Customs Union in exchange for an agreement by Russia to step back from retaliating against Ukraine for signing a DCFTA with the EU.

## Constraining Putin

While the overall thrust of EU policy on Russia should be centred on further developing co-operation, the EU-Russia relationship will continue to be troubled by problems related either to Russian domestic policies or to the post-Soviet space. In fact, although Russia may be post-BRIC, a stagnant Russia could be a more aggressive one if elites decide to use nationalism to mobilise domestic support. In addition, Putin has not abandoned his claim of regional hegemony in the post-Soviet space and will ruthlessly exploit EU weakness and opportunities should they emerge. Therefore, at the same time as deepening co-operation with Russia, the EU should create disincentives for the Russian elite to violate human rights, while also constraining Russia’s claims to a “lily-pad” empire in the post-Soviet space. To achieve this, the EU should:

- **adopt a visa ban and asset freeze for those involved in the death of Sergei Magnitsky.** The EU should adopt legislation similar to the US Justice for Sergei Magnitsky Act 2011, as the European Parliament and the Dutch Parliament have urged. Member states should follow the US and blacklist those involved in gross human rights violations.<sup>88</sup> The EU should therefore both make

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<sup>88</sup> The UK Home Office is said to have banned an unspecified number of Russian citizens deemed to be involved in the Magnitsky case from travelling to the UK. However, government officials have not officially confirmed the existence of such a visa ban. See Mark Townsend, “Secret visa bans over death of Russian whistleblower Sergei Magnitsky”, *Guardian*, 1 October 2011, available at <http://www.guardian.co.uk/world/2011/oct/01/visa-bans-russia-sergei-magnitsky>.

it easier for normal Russians to travel to Europe and harder for those that abuse power. This will not turn Russia into a democracy overnight but it could increase the cost of human rights abuses in the calculations of officials.

- **support implementation of the energy *acquis* in the neighbourhood.**

Both Moldova and Ukraine have recently joined the European Energy Community, which should extend the provisions and rules of the EU common energy market to them. However, without strict implementation of the EU *acquis*, Moldova and Ukraine will not get the full benefits of such an arrangement, not least in terms of reducing their energy vulnerability towards Russia. The EU should therefore prioritise support for gas and electricity interconnectors with Ukraine and Moldova, while also offering assistance in the implementation of the energy *acquis*. This would mean that the EU's energy legislation, liberalisation of the energy market and competition policies in this sector would be fully applicable and could, in return, protect to a certain degree Kyiv and Chisinau from Russian energy pressure. In order for the enforcement of EU rules to be credible and effective, Kyiv and Chisinau could also grant the European Commission the right to police the application of EU rules in Moldova and Ukraine by investigating in co-operation with local authorities those actors suspected of anti-competitive behaviour and market monopolies.

- **expand security co-operation with the EU's eastern neighbours.**

The EU should continue efforts to solve the protracted conflicts in the region, while continuing the Meseberg process of enhanced security co-operation with Russia in exchange for concrete progress on conflict settlement in Moldova. Apart from some specific issues, the EaP currently lacks a security dimension, leaving one of the key components of Russia's "lily-pad" empire unaddressed. The EU should create an EaP security basket focusing on concluding agreements with all willing EaP states on crisis-management co-operation, promoting legal reform of security sectors and their accountability and transparency, as well as tackling soft-security threats and co-ordinating peacekeeping contributions with increased access to EU military academies. Many of these functions are part of NATO Membership Action Plans (MAP), which are currently off the cards for neighbourhood countries. Individual member states should be encouraged to conclude bilateral security partnerships with EaP countries that have demonstrated commitment to reform, such as Georgia, Moldova or Ukraine. The EU should also use EaP high-level security platforms to sponsor meetings between EU and neighbourhood defence ministers and involve neighbourhood states in European military officers exchange schemes (the "military Erasmus").

- **make Russia an issue in EU-China relations.** The EU and China have overlapping interests in seeing Russia advance towards better rule of law and economic openness and less corruption, and have recently signed their own Partnership for Modernisation. Thus Beijing and Brussels could launch an informal dialogue on how best to pursue common objectives in a more co-ordinated manner.

Standing at the edge of the abyss of the gravest economic crisis since the 1930s, foreign policy towards Russia may not seem like the EU's highest priority. But with the US increasingly focused on the Pacific, it is now more imperative than ever that EU member states develop a coherent approach towards Russia. Developing a strategy for a post-BRIC Russia could help stop the EU's economic troubles leading to foreign-policy disintegration. Without such a strategy the EU risks being once again outplayed, in the neighbourhood and beyond, by a more cynical if committed player despite his weaker hand: Vladimir Putin.

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