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**POWER AND UNEVEN GLOBALIZATION  
Coalitions and Energy Trade Dependence  
in the Newly Independent States of Europe**

Corina Herron Linden

A dissertation submitted in partial fulfillment of the requirements of the degree of

Doctor of Philosophy

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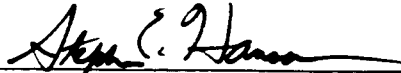
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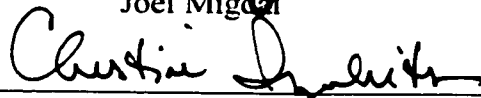


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Abstract

Power and Uneven Globalization:  
Coalitions and Energy Trade Dependence  
in the Newly Independent States of Europe

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The economies of the European former Soviet Union were dependent upon energy subsidies in the form of virtually free oil and natural gas imports from Russia, the loss of which implied dramatic shocks to domestic production structures, and the maintenance of which implied continued policy concessions to Russia. Yet some of these states actively pursued integration into the global economy while others sought to maintain the shelter of domestic markets and Russian energy subsidies. While the economic costs of openness and restructuring would be high in all cases in the short term, it is the *political* costs of openness and restructuring that determine the policy of the state. Where the high costs of restructuring are borne by a politically disenfranchised group, a consensus coalition can emerge in favor of rapid restructuring and energy reorientation. Where the benefits of the status quo accrue to a well-organized coalition closely allied with the state, a consensus coalition emerges in favor of maintenance of energy subsidies from and political relationship with Russia. Where the costs of restructuring are borne

broadly or by a well-organized minority group, power oscillation and fragmentation will lead to inconsistent policy and slow progress toward energy reorientation and reform.

Integrating a state-in-society approach to coalition formation within the field of international political economy, the author argues that states dominated by globalist-liberalizing-nationalist coalitions were able to implement energy trade reorientation by politically disenfranchising the ethnic minorities who populated the sector most vulnerable to energy contraction, heavy industry. These “globalizers,” Estonia and Latvia, bore the high costs of restructuring industries and importing energy at world prices. Belarus, dominated by pro-Moscow-statist-leftist coalitions, sought to preserve energy subsidies through political and economic reintegration with Russia. States ruled by divided governments or an oscillation of power failed to implement either policy consistently, resulting in continued energy dependence on Russia. Lithuania, Moldova, and Ukraine, the “hybrids,” sought to limit their energy dependence on Russia, but could not meet their energy needs at world-market prices. They remained dependent on Russian energy, while struggling toward energy trade diversification

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## **PREFACE**

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The territory of the former Soviet Union holds perhaps the most plentiful untapped energy reserves in the world. Collectively, the countries of the former Soviet Union are the largest producer of oil and natural gas, and the third largest of coal. In a global economy powered by increasingly scarce fossil fuels, this region may hold the key to sustained economic growth in the 21<sup>st</sup> century. The politics of energy among the states which inherited this wealth are inherently important to all those interested in international political economy.

The energy politics of the region are not only the politics of plenty, but the politics of dependence as well. Where pipelines and powerlines are the lifelines sustaining the national economy, energy autonomy becomes essential to *de facto* sovereignty for emerging states. The dilemmas for policy makers posed by interest groups wedded to the "old economy" are not unique to energy politics in the Newly Independent States, however; they are dilemmas familiar to any state seeking to engage the globalization process. The lessons learned here may therefore be applicable to the broader question of sectoral restructuring and the "internationalizing" of domestic economies.

Statistical data for this study are taken, where possible, from publications by international institutions such as the International Energy Agency and World Bank. Statistics were also gathered from publications by the Statistical Committee of the

Commonwealth of Independent States as well as the statistical ministries of the individual countries. In addition, special reports were prepared for this study by the statistical ministries of Estonia, Latvia, Lithuania and the Russian Federation. Information on the politics and policy of the NIS was gathered from interviews conducted with state officials, academic experts, industry leaders and political party representatives during fieldwork in Russia, Belarus, Lithuania and Estonia in 1999. Various government and academic publications on energy, economy and politics from the states in question were also utilized, in addition to secondary sources such as historical and news databases in the United States.

In chapter one, I outline both the empirical and theoretical questions posed by the differing strategies pursued by the European NIS in the post-Soviet period, and describe my argument. In chapter two, I trace the history of Russian energy trade policy in the Soviet and post-Soviet eras, the context within which the European NIS made their energy choices. In chapter three, I explain my broader findings across all six cases. In chapter four, I describe the globalizers, exploring the Estonian case at length and briefly addressing the secondary case of Latvia. In chapter five, I investigate the case of a hybrid, Lithuania, and provide summaries of the secondary hybrid cases of Moldova and Ukraine. In chapter six, I explain the case of the Russophile, Belarus. In chapter seven, I outline the broader implications of the findings of the study.

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*For Greg.*

*Love is ever the beginning of knowledge, as fire is of light.*

*-- Thomas Carlyle*

## CHAPTER I

### INTRODUCTION: INDEPENDENCE AND “POWER” POLITICS

#### I. Introduction

Why does one state suffer the contraction and unemployment resulting from economic opening while another, similarly positioned state chooses protection? Why is one state willing to sell *de facto* national independence for the economic stability and security of cheap oil and natural gas while states sacrifice vast economic sectors in order to attain it? Why have some states been successful in maintaining pro-market policies while others have become mired in dysfunctional economic systems somewhere between “planned” and “market”? These are some of the central questions raised by the post-Soviet experience of the European Newly Independent States.<sup>1</sup> The economies of the European Newly Independent States were dependent upon Russian energy subsidies, the loss of which implied dramatic shocks to domestic production structures. Yet some of these states have actively pursued integration into the global economy while others have sought to maintain the shelter of domestic markets and Russian energy subsidies. The economic costs of openness and restructuring would be high in all cases in the short term. I argue that it is the *political* costs of openness and restructuring that determine the policy

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<sup>1</sup> For the purposes of brevity, the term “Newly Independent States” is used to signify all states which were formerly part of the Soviet Union and have subsequently become sovereign nations. This term is preferable to “post-Soviet,” as this can also be used to signify states of Eastern and Central Europe which are former members of the Soviet sphere of influence. The term NIS is somewhat problematic, however, when referring to the Baltic states, as they view their independence not as new, but rather as the reassertion of the sovereignty they enjoyed during the interwar period. The term “emerging states” may therefore be

of the state. In short, where the cost-bearers of restructuring are largely politically disenfranchised, the states will pursue globalization; where they are politically dominant, the states will seek protection.

In late 1991, the face of the world was being transformed. Two parallel processes were at work: the collapse of communism and the globalization of the international economy. The traditional classification of the globe into three "Worlds" was becoming increasingly irrelevant. Many in the West viewed the dissolution of the communist world with unadulterated enthusiasm, as the ultimate and long-anticipated victory of capitalism and democracy. It was widely assumed that it was only a matter of time and investment before the post-communist states became modern capitalist democracies, following the American or Western European model. The "Second World" had ceased to exist, and had been transformed virtually overnight into the "transitional economies." Soon the land, labor and resources of these economies would be open to the international market. The marketization of certain sectors, including and perhaps especially the vast oil and natural gas resources of the Soviet empire, held the promise of immense wealth and cheap access for Western investors and consumers.

Nearly a decade later, the fallacy and naiveté of these assumptions became evident. While a handful of these new states embraced liberalization and democratization, some remained unrepentant dictatorships. The most common outcome, however, was that of a democratic or partially democratic political regime accompanied

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more accurate, though also somewhat vacuous with no distinction from other nascent democracies and transitional economies around the world.

by a perennially mixed or hybrid economy. Investment in and operation of certain important economic sectors, particularly the energy sector, remained highly politicized.

The second process, the growing openness and integration of national economies into an increasingly seamless global economy, presented states with unprecedented opportunities -- and risks. The possibility of rapid economic growth and massive international investment was accompanied by exposure to the slings and arrows of volatile international markets and fickle foreign investors. Regions of the world, and individual states, engaged this globalization to different degrees and in different ways. The post-socialist, post-Soviet world occupied a unique position in this process.

Perhaps surprisingly, given the transformative and parallel nature of these two processes, relatively little scholarly attention was paid to the interaction of the two, that is, the place of the former Second World in the process of globalization, and the impact of globalization on the politics of these states. While much has been written about the First and Third Worlds, the former Second World was largely neglected by the field of International Political Economy. As international markets reach the final frontiers of global economic space -- the Third World and the former Second World -- the neglect by IPE scholars of the second robs us of the insights into globalization that post-communist opening may highlight, and into the unique characteristics of the communist legacy that exposure to international markets have brought into view. This study seeks to begin to rectify this omission. I wish to bring the post-communist world back into the study of international political economy, and into the study of globalization itself.

In doing so, I use the comparative method within the field of international political economy. As the international economy expands and integrates the economies of nations, much is to be learned about the nature (and limits) of that integration by comparing the reactions of different states. Specifically, I find state-in-society analysis the most illuminating lens through which to analyze the Newly Independent States in the international political economy. State-in-society analysis, however, has traditionally been applied to the Third World, and rarely with an explicit view to the international economy. Thus, my study contributes to the state-in-society literature in three ways: it expands the examination of the impact of international-level factors on state-society relations; it investigates the influence of globalization, specifically, on the relative power of different social forces and on the policies of the state; and it expands the application of state-in-society analysis further into post-Soviet space.

This study also calls into question a second set of assumptions made at the dawn of the post-communist era, those regarding the nature of the relationship between economic liberalization and political democratization. It was broadly assumed that the two processes were complementary, perhaps even necessitating one another. Instead, I find that the most economically liberalizing states of the former Soviet Union, those which engaged the globalization process most openly, were highly politically exclusionary. The most successful economic reforms have been built upon the foundation of political disenfranchisement. While political exclusion by no means ensures economic liberalization, I argue that it can in some cases help to establish and maintain such policies.

The process that has come to be known as globalization -- the growth of trade, the integration of financial markets, and the growing interdependence of the politics and cultures of states -- has not been uniform: some states have integrated rapidly into the global economy while others have remained relatively isolated. This disparity was particularly remarkable among the Newly Independent States, the former members of and successors to the Soviet Union. While these states began their existence with economies highly integrated with one another and largely isolated from the world economy, they have subsequently engaged the global economy to very different degrees.

One of the most important features of globalization is the exposure of domestic economies to brutally competitive world markets. Isolation from the international economy can provide shelter from this gale of creative destruction, protecting groups whose livelihoods are based in weak, less competitive sectors. The post-Soviet economies are particularly vulnerable to international market forces because of their infamously inefficient communist-built production structures. In addition, these production structures in the European NIS rested on the foundation of essentially free energy imports from Russia. The economies of many of these states had been transformed during the Soviet era into heavy industrial giants. This industry consumed inordinate amounts of energy, yet these European republics possessed few indigenous energy resources of their own. Their energy-dependent economies could function only as long as they continued to receive free energy from the more oil- and natural gas-abundant republics.

The Soviet Union inherited from the Russian Empire a land rich in resources, primary among them, oil and natural gas. The Soviet leadership recognized this and developed an expansive energy sector stretching from the Baltic Sea to the Pacific Ocean, from the Arctic to the Black Sea. Consistent with Soviet developmental strategy, the energy industry was highly integrated both physically and financially. Great webs of interconnected gas and oil pipelines radiated from production centers. Political and economic control over the industry was placed in the hands of the government ministry and its local subsidiaries.

This vast, integrated energy system provided discounted energy to many republics and Soviet satellite states. Energy subsidies in many cases provided the basis for industrialization and development in these regions, making projects ranging from heavy manufacturing to residential heating systems possible. The economies of the energy recipients were built and dependent upon receiving inexpensive oil and gas, primarily from Russia. To Russia, supplying cheap fuel to the republics was yet another method of insuring political and economic influence over them.

The end of the Soviet Union meant the end of monopolistic state control, but not the end of the integrated energy system. The physical infrastructure and the political-economic coalitions that comprised the Soviet fuel sector remained long after the Soviet Union itself disintegrated. The pipelines that carry Russian-produced fuel to markets in the West travel under now-independent Ukraine, which has insufficient energy resources of its own. The only pipelines to carry fuel from pumps in some parts of northern Russia

go directly to refineries in now-independent Baltic republics. Pipelines to carry Russian oil to parts of Europe must go through Belarus.

Moreover, these countries were not merely transit points through which Russian fuel is exported, but they were themselves major consumers. While their control over Russian exports, such as it was, might have given them some bargaining edge, the fact remained that their economies were vulnerable to Russian fuel stoppages. Russian threats of pulling the plug on oil and gas shipments jeopardized production, transportation and even human life in the recipient states. This was potentially very costly to the new states both in terms of economic and human losses, and in terms of loss of political legitimacy and popularity at home and abroad.

## **II. The Puzzle**

In the first post-Soviet decade, the former Soviet republics have chosen to address this legacy of dependence on Russia in different ways. Many are investigating the possibility of achieving energy autarky by developing domestic sources such as coal or nuclear energy, but (because of the lack of resources, capital, or both) few are finding this to be financially feasible. Instead, some have turned Westward toward the global market for fuel supplies in an effort to sever the Russian imperial ties. World market fuel prices are higher than those offered by Russia, making this strategy more expensive than buying from the traditional source, but less onerous than attempting to rely on domestic resources. The costs of reorientation are exacerbated by the need of many countries to build new infrastructure in order to import sufficient quantities of oil or natural gas from

anywhere but Russia. Thus, even if Russia were to charge world-market prices of these states, energy trade reorientation would still prove more costly than simply buying from Russia. In the short-term, then, both of these strategies of energy policy reorientation are more expensive than the status quo, but they may provide more political independence in the long term. Yet some states have chosen to retain Russia as their primary supplier, and primary political partner. Why do some states maintain the Soviet-era energy ties with Russia while others turn toward the global market?

We can discern three basic strategies to address this dilemma: globalizer, Russophile, and hybrid.<sup>2</sup> Estonia and Latvia – the globalizers -- chose the strategy of turning Westward, bearing the high costs of restructuring industries and importing goods at world prices. Belarus – the Russophile --pursued the opposite strategy, and sought political and economic reintegration with Russia. Lithuania, Moldova and Ukraine – the hybrids -- sought to limit their energy dependence on Russia, but could not afford to feed their energy needs at world-market prices. They continued massive energy imports from Russia, despite other indications of an interest moving out of Russia's shadow and while struggling toward energy trade diversification.

This strategy divergence among the European NIS might be explained by many factors. One explanation might be that the states simply face a different set of incentives

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<sup>2</sup> For want of a better term, "hybrid" will be used to describe the strategy which combines both attempts at globalization and the maintenance of energy subsidies from Russia, facets of both the market and state-planned economies. Many terms have been used to refer to this group of states, including "transitional," "intermediate," "gradualist," etc. All of these terms imply a unilinear march toward marketization, which may be contradicted by the possible sustainability of these somewhat dysfunctional economic systems. Instead, I will adapt the term "hybrid" from Stephen Hanson's article "Analyzing Post-Communist Economic Change." *East European Politics and Societies* V. 12, No. 1, Winter 1998 (p. 169), to refer to this new type of system.

based upon natural resources and geographical location. Perhaps there is some idiosyncrasy of the pipeline distribution infrastructure that makes it advantageous for some states to maintain their trade relationship with Russia while others look elsewhere. This explanation is weak, however, in that our cases share similar geostrategic locations (between Russia and Western Europe) and resource endowments (poor), yet are pursuing different courses with respect to their energy trade. Energy infrastructural differences, such as the existence or absence of pipelines, ports or secondary domestic resources, also do not correlate well with outcomes. Other explanations might include sectoral composition, relative affluence, degree of trade openness, geographical proximity to Western Europe, cultural tradition or affiliation, or history of animosity with Russia, or of independent statehood. For reasons outlined below, none of these factors satisfactorily explains the post-independence variance among the European NIS.

The economic sectoral composition of all the European NIS (with the exception of Moldova) was dominated by heavy industry. Moldova alone was predominantly agricultural. While industry in Ukraine was the largest sector of the economy, it was generally based in older technology than were the industrial sectors of Belarus, Latvia, Lithuania and Estonia. These four states were among the most industrialized in the Soviet Union, with some of the most modern and technologically advanced industry in the Union.<sup>3</sup> Based on sectoral composition, then, one would expect Moldova to exhibit the most divergent strategy. One would expect similar outcomes of Belarus, Lithuania,

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<sup>3</sup> Economist Intelligence Unit, *Country Reports and Country Profiles*, 1989-1993; Interstate Statistical Committee of the Commonwealth of Independent States, *Statisticheskii Bulletin': Sodruzhestvo Nezavisimikh Gosudarstv*, 1991-1993.

Latvia and Estonia, based on their similar sectoral compositions. To the contrary, we find that Belarus is the Russophile, Lithuania is a hybrid (like Ukraine and Moldova), and Estonia and Latvia are globalizers.

Similarly, the relative affluence of the republics in the late Soviet period does not predict the outcomes well. Again, Moldova was the poorest among the European NIS. Ukraine also had relatively low NMP per capita. The remaining four enjoyed a relatively privileged status within the Soviet Union, and had NMP per capita levels well above the all-Union average. Lithuania was highest, followed by Belarus, then Estonia and Latvia.<sup>4</sup> If relative affluence were positively correlated with the degree of economic reform, one would expect Lithuania to be the leading globalizer. Belarus would be pursuing openness, and at a greater pace than either Estonia or Latvia. Ukraine and Moldova would be expected to be the most dedicated Russophiles. This is not the case, however. The degree of economic integration, or trade “openness” or “vulnerability” might be argued to explain subsequent trade strategies. In fact, all six states, like all constituent republics of the Soviet Union, were highly dependent on trade: economic integration of the republics was a central tenet of Soviet economic policy.

Geographical proximity to Western Europe might provide readier access to Western capital and export markets, facilitating economic reform and trade reorientation. This explanation correlates well for Estonia, the most advanced globalizer and the state geographically closest to the eastern borders of the European Union (in this case, to Finland). The correlation ends there, however. Lithuania and Latvia are approximately

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<sup>4</sup> Ibid.

equidistant from Sweden, the closest EU frontier, yet one is a hybrid and one a globalizer. Ukraine and Belarus are approximately the same distance from Germany, and yet have exhibited radically different outcomes. Moldova stands alone as the furthest from the capital markets Western Europe, and would therefore be expected to be the Russophile. Instead, it is, in fact, a hybrid.

Some have argued that the different paths the European NIS have chosen grow from deep historical cultural affinity, or antipathy, to the great powers around them. Cultural arguments can be difficult to evaluate, as culture itself is often an ill-defined variable. As imprecise as measures and indicators may be, it is nonetheless important to address this issue. Cultural affiliation and similarity may perhaps best be judged by long-standing and deeply integrated reflections (and determinants) of that culture, namely, linguistic and religious similarities and differences.

Let us first examine linguistic similarities between Russia and the European NIS. The Slavic languages, also called Slavonic languages, are a subfamily of the Indo-European family of languages. Because the Slavic group of languages seems to be closer to the Baltic group than to any other, some scholars combine the two in a Balto-Slavic subfamily of the Indo-European classification. The Slavic subfamily has three divisions: East Slavic, West Slavic, and South Slavic. The members of the East Slavic branch are Russian, or Great Russian; Ukrainian, also called Little Russian or Ruthenian; and Byelorussian, or White Russian. Both Latvian and Lithuanian belong to the closely related Baltic subfamily of the Indo-European family of languages and use a writing system based on a modified Roman alphabet.

Linguistically, Belarus is clearly most similar to Russia. Byelorussian is a Slavic language very similar to Russian. While some debate whether it is actually a separate language or merely a dialect of Russian proper, there is enough of a difference between the two languages to inspire a debate as to which should be the official language of Belarus. Some Belarusians, apparently, discern an important difference. Ukrainian belongs to the family of Slavic languages as well, though it is less similar to Russian than is Byelorussian. The Moldovan and Estonian languages, however, are not members of the Balto-Slavic family. Moldovan is most similar to Romanian, which is a member of the Romance group of the Italic subfamily of the Indo-European family of languages. Estonian is a Finno-Ugric language, most closely related to Finnish. Finno-Ugric is the major branch of the Uralic family of languages, subdivided into Finnic, which includes Finnish and Estonian, and Ugric, which includes Hungarian. Based on linguistic similarities, we would expect Ukraine and Belarus to keep their close ties to Russia; Latvia and Lithuania to be hybrid cases of the same type; and Estonian and Moldova to be “Westernizers”. This does not fit the actual outcomes well.

While religious practice was actively suppressed by the communist regime of the Soviet Union, it has seen a resurgence in many of the newly independent states. Ukraine is traditionally orthodox Christian, as is Belarus. However, there are large communities of Pentecostal Christians in Ukraine, and the fastest-growing religion in Belarus, particularly in the west, is Catholicism. Moldova is predominantly Eastern Orthodox. Lithuania is primarily Roman Catholic. The largest religious group in Latvia is Lutheran, along with Roman Catholic and Russian Orthodox. In Estonia, the largest group is

Lutheran, followed by Russian Orthodox and Estonian Orthodox. Religion on its own does not fit outcomes well, particularly in the hybrid cases. Lithuania is a hybrid case, but should be as “western” as Latvia and Estonia, and yet in outcome is more similar to Ukraine and Moldova. Belarus, the Russophile, is increasingly “western” in terms of religion.

It could be argued that it is important to examine the history of the state in terms of the length of time it was ruled by Russia or the Soviet Union, and its history of independent rule. In some circles, it has been conventional wisdom that the Baltic states were more independent of Russia because they were not conquered by the Soviet Union until the beginning of WWII, while the other states passed more or less directly from the hands of the Russian Empire into those of the Soviet Union. This conception of the region’s history is somewhat misleading, however. While Latvia, Lithuania, and Estonia were independent states during the inter-war period, roughly from 1919 to 1940,<sup>5</sup> they had previously, like the other states in this study, all long been subjects of the Russian Empire. Likewise, portions of Moldova remained independent during the interwar period as well.

Furthermore, this brief 20-year interlude was virtually the only period of independence in the history of the Latvian and Estonian states. Estonia was ruled by the Livonian Teutonic Knights from the thirteenth through fifteenth century. It was then conquered and ruled by Sweden until Sweden’s defeat by Peter the Great in 1721, when Estonia became a part of the Russian Empire. Latvia was also ruled by the Teutonic

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<sup>5</sup> A period preceded by brief, if devastating, German occupations around 1918-1919.

Knights, then by Poland, then, like Estonia, by Russia. Of the Baltic states, only Lithuania has a history of prolonged, powerful independence, albeit a distant history. Lithuania was one of the leading states of medieval Europe, ruling a domain that stretched from the Baltic to the Black Sea. It merged with Poland in the sixteenth century and, like the other Baltic states, became a subject of Russia in the eighteenth.

Belarus, like Estonia and Latvia, has only a short history of independence. Belarus was ruled by Lithuania, then by Poland in the sixteenth century. It became part of the Russian Empire in the 1770s, as did the Baltic states. Belarus became part of the USSR in 1918 and remained so for the inter-war period. Ukraine was ruled by Poland until a brief period of independence in the seventeenth century, after which it was, like the others, swallowed up into Russia in the eighteenth century. Ukraine declared independence in 1917, but this independence was short-lived. It was incorporated into the USSR in 1922. Likewise, Moldova has been the object of numerous invasions and territorial realignments, and has been part of Romania, Ukraine, and the Soviet Union.

An inverse argument may also be made: the legacy of imperial domination by Russia and suffering at the brutal hands of the Soviet regime can provide the impetus for rebellion against those powers. The greater the historical suffering, the greater the fuel for independence. In fact, all of the nations in question have significant historical justification for animosity toward Russia. The Baltics, Ukraine, and Belarus all suffered greatly under Stalin during WWII, and the latter two endured his earlier scourges of collectivization and purges as well. Why are they all not equally turned against Russia, then, when they share this legacy of victimization and oppression? The identification of

the "nation" as Eastern or Western has more to do with contemporary politics than with the fact of historical oppression by Russia, as does the definition of Stalinist oppression as specifically "Soviet" or "Russian." Visions of national identity with competing interpretations of affinity or enmity with Russia exist within each of these states. Which vision "wins" and comes to be reflected in policy is a matter of coalitions and bargaining, a matter of *politics*.

### III. International Political Economy Theory

Perhaps surprisingly, analysts in the field of international political economy have not yet devoted much attention to the question of relations among the post-Soviet states.<sup>6</sup> This is surprising because these cases provide such interesting examples of the effects of economic integration and *disintegration*, and the effects of domestic coalitions and

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<sup>6</sup> A preliminary assessment of Russia's place in globalization is made by Vladislav Zubok, whose conclusions center on Russia's failure to engage the globalization process:

"The Russian economy has to go through a long and painful process of complete restructuring before massive foreign investment (as distinct from foreign aid) will come and before Russian-made goods will enter the world market... The economic problems are compounded by the failure of the Russian presidency and the parliament to generate a coherent industrial and trade policy. So far the state has not been able to establish a proper framework for international business in Russia (financial infrastructure, norms, and regulations) conducive to business activities and investments." (Holm and Sorenson, p. 110.)

Zubok's argument is typical of this literature in viewing Russia (and perhaps by extension, since these are largely institutional arguments, also the NIS) as the negative case in the integration literature. However, these broad-brushed explanations get us no closer to solving variance among the post-Soviet cases.

Peter Rutland, in "Count Them Out or Count Them In? Post-Socialist Transition and the Globalization Debate" puts us on the right path:

"Increasingly, the relevant paradigm for understanding the economic development in Russia and the other newly-independent states will not be a centrally-managed transition model, but an inchoate process of contradictory and competing political and economic trends, played out across Eurasia's vast regional mosaic." (Rutland, p. 8.)

However, Rutland's work is still preliminary, and is more of a manifesto for investigation than an explanatory framework per se.

See Vladislav Zubok, "Russia: Between peace and Conflict," in Hans-Henrik Holm and Georg Sorenson, *Whose World Order? Uneven Globalization and the End of the Cold War* (Boulder, CO: Westview Press 1995), and Peter Rutland, "Count Them Out or Count Them In? Post-Socialist Transition

institutions on economic relations and "globalization" -- both central questions in the field of international political economy. These countries could potentially serve as sources of new data and new case studies in a field constantly constrained by the limited number of cases available. Even in recent volumes on the limitations of globalization such as Andrew Gamble and Anthony Payne's *Regionalism and World Order*, and Suzanne Berger and Ronald Dore's *National Diversity and Global Capitalism*, the NIS receive scant attention. Because a relatively small number of international political economy theorists have focused on this area, many "competing explanations" for the puzzle in question must be extrapolated from established schools of theory rather than drawn directly from individual analysts' work.

### *Mercantilism*

The mercantilist school of international political economy sees the pursuit of relative power and the struggle for survival in an anarchical system as the driving forces behind state action. Some mercantilists have examined the politics of international energy markets, often inspired by the oil shocks of the 1970s. Most notable among these is Steven Krasner's *Defending the National Interest*,<sup>7</sup> in which he examines the U.S. government's response to threats to American oil and raw materials investments abroad. Krasner implements a more sophisticated analysis of the origins of state preferences and the role of society in state policy than do most mercantilists. But while Krasner argues

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and the Globalization Debate," prepared for the American Association for the Advancement of Slavic Studies, 1999.

<sup>7</sup> Steven Krasner, *Defending the National Interest: Raw Material Investments and U.S. Foreign Policy* (Princeton: Princeton University Press, 1978).

that we must define state interests inductively rather than deductively, the state preferences he defines are virtually identical to those which another mercantilist might deduce from the state's position in the international power structure. This study seeks to explain why those preferences might differ. And while Krasner sees that the interests of the society can diverge from those of the state, he ultimately finds that the state almost always acts according to its own preferences, often despite the objections of social groups. This study seeks to explain how the state's preferences and policies are fundamentally defined and constrained by society. For our purposes, because the boundaries and preferences of the states themselves are evolving simultaneously with their policies, we need a more nuanced understanding of state-society relations than Krasner offers. Secondly, while Krasner *is* addressing the topic of international oil markets, he is examining the question of the protection of foreign assets by a superpower rather than the dependence on imports by rather small, less powerful states. The structural problems facing the latter fundamentally differ from those facing the former, and are of central importance to the construction of a mercantilist argument.

Since mercantilists have not directly addressed our cases, their arguments must be extrapolated from the canons of the literature. Mercantilist analysts would expect the smaller states to attempt to reduce their sensitivity and vulnerability to interruptions in energy supplies from Russia. Their dependence on Russia for such an essential good would be seen as a threat to national security and prosperity, undermining the state's political autonomy both internationally and domestically. Moreover, the economic

decline of Russia as the regional hegemon would undermine its willingness and ability to enforce the previous trading regime.<sup>8</sup>

The goal of decreasing vulnerability could be achieved in two ways: states could seek autarky through development of indigenous energy resources such as coal, oil shale, or nuclear reactors. If this proved unfeasible, a second (albeit less desirable) alternative would be to diversify suppliers. By cultivating energy trade with both East and West, the state may hope to make itself less vulnerable to the whims and wants of either. Moreover, states would see the advantage of bandwagoning with the increasingly powerful West over remaining in the shadow of the declining and dilapidated Russia. Some European NIS have pursued this strategy, but by no means all. Mercantilist analysts emphasize system-level, that is, international factors in their explanations. For most mercantilists, the state is a "black box" into which we may not peer. Since the six European NIS faced very similar external opportunities and constraints, mercantilism would have great difficulty accounting for the diversity of outcomes.

### *Neo-Marxism*

Neo-Marxist theorists such as dependency and world-systems analysts would argue that these semi-peripheral states would have little choice in re-orienting their economic and political ties to the core.<sup>9</sup> There has been some recent work among world-

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<sup>8</sup> Stephen Krasner "Structural Causes and Regime Consequences: Regimes as Intervening Variables" in *International Regimes*, Stephen Krasner, ed. (Ithaca: Cornell University Press, 1983), Stephen Krasner "State Power and the Structure of International Trade" *World Politics* 28, n.3, and Robert Gilpin *Political Economy of International Relations* (Princeton, NJ: Princeton University Press, 1987).

<sup>9</sup> In this analysis, it is the core states, and the trade structure that supports them, that have the power. The "agency" allowed peripheral and semi-peripheral states is limited, at best. [See: Fernando Cardoso and

systems theorists which addresses the NIS more directly.<sup>10</sup> There is broad agreement among world-systems theorists that the successor states of the Soviet Union, including Russia, fall into the semi-periphery.<sup>11</sup> According to this model, one would expect that

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Enzo Faletto, *Dependency and Development in Latin America* (Berkeley, CA: University of California Press, 1979). Andre Gunder Frank, "The development of underdevelopment" *Monthly Review* Sept. 1966 v.8. Immanuel Wallerstein *The Modern World System: Capitalist Agriculture and the Origins of the European World Economy in the Sixteenth Century* (New York: Academic Press 1974), and Immanuel Wallerstein, "The Rise and Future Demise of the World Capitalist System: Concepts for Comparative Analysis" *The Capitalist World Economy* (New York: Cambridge University Press, 1979).] In later versions of these theories [see Peter Evans *Dependent Development: the Alliance of Multinational, State, and Local Capital in Brazil* (Princeton, N.J.: Princeton University Press, 1979) and *Embedded Autonomy: States and Industrial Transformation*. (Princeton, N.J.: Princeton University Press, 1995)], domestic elites in peripheral countries may exact concessions from international capitalists, or may cooperate with them to their mutual benefit. States may, if they possess the institutional capacity, turn foreign capitalists' activities to their developmental advantage. But these states have limited bargaining power in terms of turning core states away. In short, extrapolation from these arguments would lead us to conclude that the energy and trade orientation of the former Soviet satellites would have more to do with the international economic structure and the richer nations than it would have with the policies and desires of the post-Soviet periphery.

Dependency theory assumes little variation on the part of peripheral states. These states, initially forced into integration with the capitalist economy through colonization, become trapped in a dependent relationship with the core. They export raw materials and other low value-added goods to the core states, import capital and high value-added goods, getting squeezed by the vices of capital flight and declining terms of trade. Because all of the power in this relationship rests with the core, it is difficult to construct an explanation of why some peripheral states choose some trade relationships over others. There is little choice in the matter.

<sup>10</sup> There is some disagreement among these theorists as to how to categorize the Soviet Union – as semiperiphery within the capitalist world-system, or as self-contained, competing world-system. Some argue that the Soviet Union and its satellites were a failed attempt to change the structure of the world-system from capitalist to socialist. A different view, which is gaining increasing acceptance, is that the Soviet Union was itself not truly socialist, and rather than posing a serious challenge to global capitalism was itself subsumed into the capitalist world-system as semi-peripheral states. The Soviet Union, particularly after the 1960s, became more integrated into the capitalist world-system through its dependence on exports of raw materials and imports of capital and technology from the core. The Soviet Union erected trade barriers and protected domestic industries in order to facilitate domestic development and ascend to the status of a core state. All of these are characteristics of the semi-periphery. Of course, the Soviet Union did differ from other semi-peripheral states in many ways, perhaps the most interesting of which being that its relationships with its satellites, while economically exploitative, were at the same time a financial burden on the Soviet Union. See recent works by Christopher Chase-Dunn (with Thomas D. Hall), *Rise and Demise: Comparing World-Systems* (Boulder, CO: Westview Press, 1997), *Socialist States in the World System* (Beverly Hills, CA: Sage Publications, 1982), and Immanuel Wallerstein *The Age of Transition: Trajectory of the World-System 1945-2025* (Atlantic Highlands, N.J.: Zed Books, 1996) and *Geopolitics and Geoculture: Essays on a Changing World-System* (New York: Cambridge University Press, 1991).

<sup>11</sup> Some of the Asian NIS are seen as peripheral states, while a few former European satellite states – East Germany and perhaps the Czech Republic – may be considered members of the core. However, all of the states of this study, including Russia, should reside in the semi-periphery.

these states, based on emerging elite coalitions of the military, large industrialists and resource-exporters, and the state bureaucracy, would emerge as semi-peripheral satellites of the Western European core. These states, because of their proximity, low wages and relatively low level of technology, would become exporters of unsophisticated manufactured goods, agricultural products and (in the case of Russia, at least), raw materials to Western Europe, in exchange for capital and technology.

These two sets of interrelated expectations – that emergence of particular forms of domestic coalitions and increasing economic integration with Western Europe – are met in the European NIS, but to differing degrees and with the opposite relationship to that predicted by world-systems theory. These coalitions are found most strongly in Belarus, with a weaker presence in the hybrid cases, and the weakest of all in Latvia and Estonia. We find that the degree of economic development and engagement with the Western European core, the supposed result of these coalitions, is instead strongest in Latvia and Estonia, moderate in the hybrid cases, and weakest in Belarus.

A second problematic aspect of the world-systems approach to the NIS is explanation of the variance in outcomes across these cases. We observe very different trajectories in development among these states, from stagnation in the semi-peripheral status to the real possibility, particularly in the cases of Latvia and Estonia, of ascension to a rarified semiperipheral status or even into the core. These states have engaged in a process of economic transformation which has caused them to shed many “peripheral” characteristics in favor of “core” characteristics (increasing wages and technology levels, decline in low-technology manufactures and agriculture in favor of services and higher-

tech production). These states are also fast-tracked for membership in the European Union, the Western European core itself.

According to world-systems theory, ascent among economic strata is a rare and difficult task. To ascend, states must gain the necessary autonomy from the constraints of the world-economy in order to erect the protections necessary for development of the domestic economy. Several sets of conditions are necessary for such ascent. First, international conditions must be favorable. This means that the semi-peripheral country must possess the state and military strength to wrest autonomy from the world-system, or the core must tolerate and even sponsor the protectionism and the ascension. While none of the states in question is militarily powerful, it might be argued that the core of Western Europe and the United States have accepted and encouraged the integration and growth of many of these economies. Estonia in particular had been the recipient of massive international investment and some technology transfer, methods of core-sponsorship. This has been decidedly less true for Belarus, and Ukraine and Moldova have failed to attract the investment and technology the Baltics have. Most importantly, however, the indulgence of the core is most necessary not in terms of technology and capital, but in terms of toleration of the protectionism of the ascending semi-peripheral states. This is not an accurate description of Western Europe's and the United States' relationship with the European NIS, as the ascending states are by far the most open and least protectionist, while the stagnating ones are more protectionist.

According to world-systems theory, domestic conditions must also be favorable. The relationship of the state to domestic capital must be supportive, but not subservient.

This is truer of Estonia and Latvia than of the other states. This is not enough, however, to validate world-systems theory: world-systems theorists argue that the ascension is driven by those who favor the protection of domestic industries from less expensive core-produced goods. Yet this domestic condition is best met in those states showing the fewest signs of ascension, and least true of those whose economies are developing most quickly.

### *Constructivism*

A third school of International Political Economy sees national security and international cleavages in the post-Cold War era as rooted in notions of national identity. It is difficult at best to definitively argue that individual national cultures have a greater affinity for one or another. Is "nation" a matter of linguistic similarity, a common religion, or history of shared government/colonization? As was discussed earlier, direct extrapolation of cultural affinity from linguistic, religious, historical, etc., similarity does not correlate well with our outcomes. Much of the recent work in IPE on national identity recognizes the difficulty in arguing for static or inherent national identities, and focuses on identity as constructed rather than primordial or "given." These ideational variables have causal significance, and come to define both "nation" and "interests."<sup>12</sup>

This "identity" seems to be highly malleable, however. There is some agreement among the constructivists concentrating on Russia, for example, that there was a dramatic

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<sup>12</sup> Peter Katzenstein argues that interests cannot be taken for granted. He argues that political and collective identities help to explain how actors define their interests, and therefore must be analyzed in conjunction with institutions and other traditional subjects of political economy research. Peter

change in Russian foreign policy in 1993, from viewing the West as partner to viewing the West as the “other.”<sup>13</sup> This change was accompanied by a change in the view of Russian identity from Western to separate from the West. While these arguments address changes in Russian, not NIS, foreign policy, they do nonetheless have applications for our study: if the identity of Russia can make such a dramatic shift, from pro-West to anti-West, in such a short time, this is a strong argument for the malleability of identities (as “Western” or “Russophile”) in the near abroad. This type of argument makes the question of changes in dominant coalitions and so-called “identity-entrepreneurs” essential.

Perhaps most importantly, the change in “identity” in Russia was driven by underlying changes in the relative strength of competing interest groups. Medvedev acknowledges that these constructions of identity were related to, and largely explained by, material interests. Medvedev argues that the change in Russian identity was driven by domestic political and economic forces: those who had benefited from the privatization process, particularly the state-oligarch coalitions who had gained control of the industrial, export and natural-resources sectors, wanted to solidify their gains. These political *and economic* variables become essential to the explanation of Russian foreign

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Katzenstein, ed., *The Culture of National Security: Norms and Identity in World Politics* (New York: Columbia University Press, 1996).

<sup>13</sup> Ted Hopf edits a volume exploring constructivist explanations of Russian foreign policy. The articles pose very different explanations of Russian foreign policy, including rejections of constructivism in favor of neorealist and neoliberal arguments. Ted Hopf, ed., *Understandings of Russian Foreign Policy* (University Park, PA: Pennsylvania State University Press, 1999) Sergei Medvedev, the author of the article, views this in terms of a move from “Culture One” to “Culture Two”. One can observe such cycles far back in Russian history, in oscillations between so-called Russophiles and westernizers.

policy, as they explain the identity shift, which accompanies the change in foreign policy. The economic and ideational interact, and are both important causal variables.

"Cultural" and "national" identities, especially in the post-Soviet context, are not *reassertions* of historic identities, but rather *reinterpretations* of them.<sup>14</sup> To this extent, we can accept conventional constructivism. However, constructivists often underestimate the importance of material factors. Cultural and identity-based arguments regarding the affinity with Russia or the West are not given, but rather negotiated. These ideational variables, along with economic ones, together come to define coalitions and ultimately the policies of the state.

#### *Inside the "black box"*

Finally, there are the scholars who believe that in order to understand a state's international policy, we must first understand its internal politics. This school is referred to in the IPE literature as a subset of the liberal paradigm,<sup>15</sup> as the "Second Image,"<sup>16</sup> or

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<sup>14</sup> Alexander Motyl's *Dilemmas of Independence: Ukraine after Totalitarianism* (New York : Council on Foreign Relations Press, 1993) is an excellent study of the construction of Ukrainian national identity after the collapse of the Soviet Union, as is Anatol Leiven's *The Baltic Revolution: Estonia, Latvia, Lithuania, and the Path to Independence, 2<sup>nd</sup> ed.* (New Haven : Yale University Press, 1994) of national movements in Estonia, Latvia and Lithuania. John Breuilly, in *Nationalism and the State* (Manchester, England: Manchester University Press, 1982), argues that competing versions of nationalism are taken up by political movements and even by the state in order to justify certain policies. Benedict Anderson in *Imagined Communities: Reflections on the Origin and Spread of Nationalism* (London, England: Verso Editions/NLB, 1983) and Ernst Gellner, in *Nations and Nationalism* (Oxford, England: Blackwell, 1983), also explore the modern origins of nations, although with less emphasis on the machinations of political elites.

<sup>15</sup> Classical liberals would expect states to produce, import and export goods based primarily on the relative prices of those commodities. If Russian oil prices were the lowest, whether because of a comparative advantage in producing oil or because of subsidies, neo-classical liberals would expect these states to purchase their energy from Russia. If the world market offered a better bargain, the states would be expected to reorient their energy imports. But if Russian energy prices are the same to all of the European former Soviet states, and are consistently lower than world prices (whether because official prices are lower or because energy may be obtained on credit), a liberal would expect all of these states to

sometimes simply as "Domestic Politics." But as any good comparativist understands, there is more than one theory of domestic politics. The Second Image literature of international political economy can be divided into two approaches: those which place the explanatory weight in the institutions of the state, and those which look at the dominant economic sectors and political coalitions.

Robert Keohane and Helen Milner provide a compelling account of the power and limitations of "internationalization" and its interaction with domestic institutions.<sup>17</sup> Internationalization affects, and is in turn affected by, domestic institutions. "The existing institutional context conditions the incentives facing interest groups and politicians."<sup>18</sup> There are several limitations to the application of this approach to the NIS cases. First, trade reorientation in these cases is not necessarily "internationalization" as Keohane and Milner define it, as it does not necessarily imply changes in trade volumes, but rather in trade *direction* and *partners*. The NIS were already highly "internationalized" economies at the time of independence, if one counts (as one must) trade with Russia and the rest of the former Soviet Union. Second, while very different

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maintain their trade relationship with Russia. Only differences in pricing, taking into account the costs of switching suppliers could explain the variety of actual post-Soviet energy policies. For classical liberal arguments on trade, see Davis Ricardo "On Foreign Trade" *The Principles of Political Economy and Taxation* (New York: E. P. Dutton & Co. Inc., 1960), Adam Smith "On the Principle of the Commercial or Mercantile System" and "Of Restraint Upon the Importation from Foreign Countries of Such Goods as Can Be Produced at Home" *The Wealth of Nations* (New York: Modern Library, 1937).

<sup>16</sup> There is also a literature that explores the impact of international factors upon domestic politics. See Peter Gourevitch, "The Second Image Reversed: The International Sources of Domestic Politics," *International Organization*, Autumn 1978.

<sup>17</sup> Keohane and Milner define internationalization as changes in trade levels as a percentage of GNP or the ratio of net foreign investment to total domestic assets. This process is generated by shifts in the underlying transaction costs, producing flows in capital, goods, and services. Robert Keohane and Helen Milner, eds., *Internationalization and Domestic Politics* (Cambridge University Press, 1996), p 4.

<sup>18</sup> Robert Keohane and Helen Milner, eds., *Internationalization and Domestic Politics* (Cambridge UP, 1996), p 5.

institutional forms have developed in the NIS since independence. the NIS states began their transitions (or lack thereof) with virtually the same set of domestic institutions. Keohane and Milner acknowledge that institution-formation is an inherently political process. "Political institutions reflect domestic actors' policy preferences, since they are internationally created to guarantee the pursuit of particular policies. But they also have independent effects."<sup>19</sup> But in our cases, the creation of institutions is part and parcel of the political struggle between vying coalitions. In the beginning, these states faced virtually the same institutional environments. Very different forms of institutions came to be established, and once established, imposed constraints on the domestic political actors. But the creation of these institutions is something to be explained, not in itself an explanation.

The Soviet Union and post-Soviet cases have taken their place in the integration and globalization literature primarily as negative cases, examples of the limits of internationalization and the affects of in international markets on domestic politics. Matthew Evangelista<sup>20</sup> argues that Soviet institution specifically proved the foil of international markets. These institutions limited both information and opportunity, blocking and refracting the impact of international markets so that many domestic actors were given stronger incentives for rent-seeking than for profit-seeking. This is a compelling argument for why the post-Soviet world has often failed to make the "transition" many ex-Sovietologists, cum transitologists, had expected. Indeed, the

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<sup>19</sup> Ibid., p 4.

<sup>20</sup> Matthew Evangelista, "Stalin's Revenge: Institutional Barriers to Internationalization in the Soviet Union," in *Internationalization and Domestic Politics*, eds. Robert Keohane and Helen Milner. (Cambridge University Press, 1996), pp. 159-185.

reform of these institutions in the post-Soviet era has proven notoriously difficult precisely because of the rent-seekers who profit from their existence. To destroy the institution would be to take away not only their livelihood, but also in many cases their power. Unfortunately for the reform-minded, those in a position to implement or obstruct reforms are often the very ones who benefit from the existing structures. These sorts of dilemmas may be observed throughout the post-Soviet world. However, this argument does not begin to address the variation among the post-Soviet states, given that they were initially all restricted by near-identical sets of market-distorting institutions. Keohane and Milner, along with Evangelista, provide a good starting point for analysis of the interaction of international and domestic politics. However, in the cases of the NIS, we must look beyond purely institutionalist and second-image-reversed approaches in order to explain the great variation in NIS outcomes.

Within this school, there are also theories of coalition formation and realignment. Ronald Rogowski<sup>21</sup> argues that the shifting political cleavages in response to changing exposure to trade can be extrapolated from the relative abundance or scarcity of the factors of production: land, labor and capital. According to Rogowski, political actors divide and realign according to their economic interest in the level of trade, producing larger political patterns such as urban-rural or class cleavages, and dominant political movements such as socialism, populism, etc. Similarly, Peter Gourevitch<sup>22</sup> studied the response of countries to exogenous economic shocks and the impact of those shocks on

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<sup>21</sup> Ronald Rogowski, *Commerce and Coalitions: How Trade Affects Domestic Political Alignments* (Princeton, N.J.: Princeton University Press, 1989).

<sup>22</sup> Peter Gourevitch, *Politics in Hard Times: Comparative Responses to International Economic Crises* (Ithaca, N.Y.: Cornell University Press, 1986).

the domestic politics of the state. Gourevitch argues that these financial crises can cause conflict among capitalists and among former coalition partners, leading to critical realignments among groups and parties. Such coalitional realignments can produce changes in economic structures, policies or even the institutions of the state itself. The role of the institutions, however, and of the state as more than a tool of society, do not play a large role in Gourevitch's theory.

Both Gourevitch and Rogowski's arguments are highly economic, as their coalitions (and cleavages) are exclusively materially-based. While Gourevitch argues that different business groups have different "marginal propensities" toward progressive or conservative realignment, this aspect remains underelaborated. But economic groups are only *a piece* of the post-Soviet puzzle: while materially-based interests are of critical importance to our understanding of dominant coalitions and energy trade preferences in the European NIS, the role of identity-based groups (and, indeed, the inseparability of the two) is also essential. How can one explain the exclusion of Russophone residents from voting, so essential to the maintenance of liberalizing coalitions and policies, without acknowledging the importance of ethnic and national motivations and interests?

Similarly, sectoral analysis tells us that we may explain the behavior of states by examining the interests of the dominant economic sectors in the domestic economy.<sup>23</sup> If this sector involves high asset-specificity and high barriers to exit and entry, the state will find it difficult to initiate policies of restructuring or reorientation that would undermine

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<sup>23</sup> See Michael Shafer, *Winners and Losers: How Sectors Shape the Developmental Prospects of States* (Ithaca, N.Y.: Cornell University Press, 1994) and Jeffrey Frieden, *Debt, Development and Democracy in Latin America* (Princeton, N.J.: Princeton University Press, 1991).

the actors in this sector. This argument is essentially economistic and society-centric.<sup>24</sup> Institutionalists argue that strong states (those with high state capacity) are able to pursue long-term, objective state interest, while weak states (those with low state capacity) may be captured by rent-seekers and are doomed to inefficient policy and economic outcomes.<sup>25</sup> This argument is state-centric both in terms of assuming the state to be an actor separate from society, and in arguing that state decision-makers' interests are identical to the long-term interests of society as a whole. Yet, I would argue that one cannot understand the relative power of sectors without examining the state institutions through which they must act, and that one cannot understand the interests of the state without looking at the interests of societal actors. Neither analytically nor factually can the two be entirely separated.

I argue that system-level (international) explanations for the differences in energy strategy fall short, and that one can explain them only with reference to the relative strength of domestic coalitions in the six countries. More specifically, when economic and identity-based coalitions that benefit from subsidized energy and close relations with Moscow are closely allied with the state, they are able to define the national interest as maintaining close ties with Russia. When coalitions that would benefit from globalization or increased economic and political ties with the West are able to ally with or capture the state, they are able to define the national interest as liberalizing and Western. The ability of these globalizing coalitions to maintain power, and their policies,

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<sup>24</sup> In addition, the Baltic states and Belarus were very similar to one another sectorally.

<sup>25</sup> Excellent applications of this approach include Peter Katzenstein *Small States in World Markets: Industrial Policy in Europe* (Ithaca, N.Y.: Cornell University Press, 1985) and Stephen Haggard *Pathways*

in the face of the displacement resulting from their liberalizing policies depends on their ability to politically exclude those groups most ill effected by these policies. When such disadvantaged groups are relatively well organized and united and cannot be politically marginalized, coalitional changes and division within the state result in conflicted and often inconsistent policies.

#### **IV. The Theoretical Framework: A State-in-Society Approach**

Viewing the politics of energy and economic reform in the European NIS through the state-in-society lens clarifies our understanding for several reasons. First, the state-in-society approach, unlike many others, does not take state preferences as given. The primary goals of the state are not assumed. Rather, the state's goals are derived from the preferences of the state actors and social forces closely allied with them. Secondly, the state-in-society approach recognizes the political salience of both economic and ideological factors. The politics of energy policy in the European NIS cannot be understood without reference to the underlying economic interests of the actors involved. But neither can the politics of energy policy be understood without analysis of the role of national and ethnic ideas which provide, in different cases, the rationale for political exclusion, for national independence, and for reintegration with Russia. State-in-society theory recognizes these processes as contested, as the stuff of politics themselves. Lastly, the state-in-society model allows us to introduce domestic-level factors into the analysis of the international political economy of energy trade in the NIS. Whereas

“international-level” factors in themselves cannot explain the outcomes of our cases, the state-in-society approach allows us to open the “black box” of the state and examine domestic politics for our explanations.

In turn, this study seeks to add to the state-in-society model as well. First, it further expands the universe of cases to which state-in-society analysis is applied. While state-in-society theorists such as Vivienne Shue have addressed the politics of China, and to a lesser extent, Russia, state-society relations in the Newly Independent States and the former Second World remain underelaborated. Second, this study further explores the interaction of international and domestic factors in the shaping of state-society relations. Scholars such as Etel Solingen have brought state-in-society analysis to bear on the question of regional order and the formation of domestic coalitions. This project seeks to build on such studies by examining not only how domestic politics shape the international and regional context, but how regional constraints shape domestic politics. Lastly, this study contributes to our understanding of how globalization shapes state-society relations, and how these relations shape, and limit, globalization itself.

The state-in-society model, as developed by Joel Migdal and his colleagues, addresses most satisfactorily the questions raised here. The state-in-society approach takes seriously both material and ascriptive bases of social and political association. It also problematizes the transformation of society, the state, and its constituent institutions, essential to our understanding of the politics of the now-independent states of former Soviet Europe. While the state-in-society approach was built to analyze the developing

world. it may help us understand the post-Soviet world as well. Migdal sees the impetus for much of the renewed struggle in contemporary international politics as rooted in the spread of world capitalism, and focuses his analytical lens on the “clashes and accommodations that these new circumstance have precipitated.”<sup>26</sup> This was written with the Third World in mind, but is equally applicable to the Second. These new states stand on the shores of the expanding global economy as well, inspiring struggles for domination, and even survival, among the “winners” and “losers” in the open market, the haves and have-nots, the empowered and the disenfranchised.

The state-in-society approach is based on the premise that our analysis of the state as a transformative force cannot take place without an examination of the social forces vying for control of the state and over one another. In fact, the state is embedded in society. According to this approach, the effectiveness of the states cannot be extrapolated from its “autonomy” from society per se, but rather is conditioned by its various ties to society. “The results of the engagement with (and disengagement from) other social forces may modify the state agenda substantially; indeed, they may alter the very nature of the state.”<sup>27</sup> Thus, while insulation from the demands of linguistic minorities may make certain policies more viable politically to a globalizer, one must at the same time examine which social forces have ties to the state, and the nature of those ties, in order to understand the policies which will emerge. One cannot make the simple argument that

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<sup>26</sup> Joel S. Migdal, Atul Kohli and Vivienne Shue, *State Power and Social Forces: Domination and Transformation in the Third World* (New York: Cambridge University Press, 1994), p. 10.

<sup>27</sup> *Ibid.*, p. 12.

state “autonomy” will lead to successful economic transformation. First one must ask, autonomy from whom?

Secondly, one must disaggregate the state. One cannot take for granted the state as a unitary actor, nor its *de facto* policies as centralized or coordinated. Because of differential pressures from social groups, top policy-makers may announce policies that are never implemented at the lower levels. The institutions of the executive and the legislature may be at odds with one another, and implement policies that work at cross-purposes. The reach of the state may indeed exceed its grasp. “The role of the state itself is an object of the struggle.”<sup>28</sup> To speak of “the” state policy, or to anthropomorphize the state as a single rational actor, may interfere with our ability to understand the origins and effects of the struggles within and for the state.

Third, one cannot take the goals of the state for granted. This is especially relevant in the post-Soviet context. Some scholars, in the early days of independence, assumed the goals of all the NIS would be to reform and to liberalize. In fact, different NIS have evidenced widely divergent state goals over time. One cannot simply assume economic transformation to be the end-goal of state policy. A number of other, potentially antithetical goals (such as social stability, economic redistribution, maintenance of an economically uncompetitive but nonetheless important power base), may indeed take precedence over this. One must also look to the social forces allied with, and penetrating, the institutions of the state in order to understand the goals and policies emerging therefrom. The state-in-society approach directs us to examine the

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<sup>28</sup> Ibid., p. 10.

social forces impinging on the state, and the relative power of the state organs and institutions *vis a vis* each other, in order to understand the goals and policies of the state.

Fourth, the state-in-society approach argues that the strength of various social forces is contingent upon empirical conditions. Unlike Marxist and materialist-liberal theories, state-in-society theory argues that class and property are not enough to predict policy outcomes. One must look to the internal organization of the social force, the level of mobilization, and the possibility of motivation around not only material but also ideational goals:

All these sorts of social forces' ability to exercise power starts with their internal organization. The efficiency of their hierarchies, their ability to use resources at hand, their adroitness in exploiting or generating symbols to which people develop strong attachments, all affect their ability to influence or control behavior and beliefs.<sup>29</sup>

A social force's ability to generate or co-opt existing symbols, its organization and its resources can all contribute to its strength. A social force may require both "material and symbolic resources in order to project a meaningful presence society-wide."<sup>30</sup>

Lastly, the state-in-society approach does not assume the state-society relationship to be necessarily zero-sum. State actors will ally with certain societal actors against other societal groups. State and social actors may work together, not necessarily against one another. In fact, it is this relationship which conditions the goals of both the state and social actors:

The multiple arenas of society and the interactions among them have been the cauldrons within which the contingent, particular historical outcomes have been brewed for each type of society. The form of the state (democracy or some other type of government), its goals, its capabilities, its scope, its domination by particular social forces or its autonomy,

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<sup>29</sup> Ibid., p. 20.

<sup>30</sup> Ibid., p. 30.

as well as the form, systems of meaning, capabilities and autonomy of other social forces – all these have been determined through these critical struggles and accommodations in the multiple arenas of society and the relationships among these arenas. States do not succeed in establishing their own domination by default. In fact, they may end up as much transformed as the transformative states.<sup>31</sup>

Of paramount importance to our understanding of the post-Soviet world is the state-in-society assertion that states and societies are “mutually transforming.”<sup>32</sup> At the dawn of independence, the NIS were states in flux: state and social institutions, political associations, geographical and ideational definitions of the nation were all in a state of change. Which social forces allied with state forces, and which were excluded, helped to define the shape and character of the new state. We cannot understand the transformation of the state (or lack thereof) without understanding the struggle to become the ruling state-society coalition.

Coalitions and accommodations may transform as well as enhance a social force’s ability to attain its goals. As a social force’s constituency changes, it may incorporate a new material basis as well as new ideas and values into its constitution. To state this point slightly different terms, in addition to a social force’s capabilities, its social and ideological basis (whom it serves and with what goals or agenda) also may change radically as a result of its interactions in an arena.<sup>33</sup>

The formation of coalitions changes and transforms the character and goals of the constituent social forces. In addition, such coalitions help to define the goals of the state, and in time of institutional change, the very nature of the state itself.

Kiren Aziz Chaudhry examines the role of both economics and identity in domestic politics. Chaudhry<sup>34</sup> builds a theory of institutional change which incorporates

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<sup>31</sup> Ibid., p. 29.

<sup>32</sup> Ibid., p. 3.

<sup>33</sup> Ibid., p. 21.

<sup>34</sup> Chaudhry, Kiren Aziz. *The Price of Wealth: Economics and Institutions in the Middle East* (Ithaca, N.Y.: Cornell University Press, 1997).

the constraints pre-existing institutions place on the process, the impact of materially-based and ascriptively-based coalitions and the impact of external shocks. While her subject matter is not transitional economies but rather Middle Eastern states and the oil market, her theory may be used to inform our understanding of transitions. For the purposes of our topic here, we are interested in Chaudhry's analysis of economic "bust" times when domestic institutional change is a matter of domestic conflict, but is shaped by the pre-bust era institutions. She argues that, counter to neoinstitutionalist expectations, Saudi Arabia, a "strong" state, was unable to implement reform because of the dense redistributive web between bureaucrats, princes and entrepreneurs as well as because of the familial and tribal ties between the state and business, all of which were institutionalized during the economic growth cycle. Yemen, a "weak" state by neoinstitutionalist measures, was able to implement some difficult economic and institutional reforms precisely because the state was separate from private business interests, both financially and ascriptively. The bureaucracy and military were staffed by the shi'i of the north, while the private economic business sector was dominated by the Sunnis of the south. This made them an easier target for extensive taxation and regulatory reform.

In the transitional post-Soviet states, notions of identity and nation are of particular importance. The totalitarian Soviet system sought to reshape all of society, including and especially the identity of its citizens. The Soviets may have failed in their 70-year campaign create *homo sovieticus*, and to subsume all national and ethnic groups into this identity, but the enterprise did leave a lasting impact. The campaigns of building

“pro-Soviet nationalism” and the use of coercion had the perverse effect of stimulating the development of *anti*-Soviet national identities, which vied with class identity (another historical irony) for the hearts and minds of the Soviet citizens.<sup>35</sup> In the struggle against Soviet rule in the late 1980s and early 1990s, the most powerful and accessible alternative identity to the “Soviet” one was that of the nation. The symbols, traditions, and language of the old regime were the natural antithesis of, the rallying point against, Soviet rule. The fact that Soviet authorities had traditionally pitted themselves against such identities only reinforced the power of the idea of the nation. Thus, Chaudhry’s integration of material and ideational, “rational” and ascriptive social groups fits well with analysis of the post-Soviet world.

While the state-in-society field has been dominated by analysis of Third World countries, a handful of scholars have begun to view the problems of the former Second World through this lens. Vivienne Shue applies state-in-society analysis to the questions of state effectiveness and reform in China. Like other state-in-society analysts, Shue does not assume the goals of the state nor that the state is a single, unified actor. Instead, both the policies of the states and their implementation at different levels of the state are subject to political negotiation. Shue emphasizes the hypothesis, also found elsewhere in state-in-society analysis, that state-society relations are not necessarily zero-sum: she argues that strong social organization can in some cases enhance the capacity of the state.

To the state-in-society field, Shue brings several new elements. First, Shue rightfully rejects the “liberal” versus “communist” dichotomy traditionally used to

categorize the post-1989 socialist world. Instead, she seeks a more nuanced understanding of how systems which fit neither mold come to be constructed of forms associated with both, and how these new systems function. Secondly, Shue investigates the specific legacy for state-society relations of a socialist experience. The patron-client relations and localist protection which evolved in response to the states' reformation of state-society relations helped define the effectiveness of the state under communism, as well as the possibility and shape of later reforms. As Shue points out, however, "as there was no single state socialism, there will be no single 'postsocialism'."<sup>36</sup> While Soviet and Maoist socialisms shared many features, they also differed significantly. The differences in their legacies are many, not least of which is the survival of China as a single, integrated state and the survival within that state of the leading role of the Communist Party. Building on Shue's analysis of the state-society relations of the socialist and post-socialist world, and on her exhortations for further research, this study introduces post-Soviet states, specifically the six Newly Independent States of Europe, into the field of state-in-society analysis. It takes seriously the structural and institutional legacies of the Soviet Union, while also seeking to explain the variation in outcomes among states with similar institutional legacies.

Etel Solingen argues that the "grand strategy" of a state and regional outcomes are based in the ruling coalitions of the states. Solingen defines a coalition as "policy networks spanning state and private political actors." Like Migdal, Solingen seeks to

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<sup>35</sup> Ronald Grigor Suny, *The Revenge of the Past: Nationalism, Revolution and the Collapse of the Soviet Union* (Stanford, CA: Stanford University Press, 1994).

<sup>36</sup> Joel S. Migdal, Atul Kohli and Vivienne Shue, *State Power and Social Forces: Domination and Transformation in the Third World* (New York: Cambridge University Press, 1994), p. 85.

avoid “purely statist notions of a completely autonomous state and purely societal-reductionist conceptions of states as instruments of society, particularly economic forces.”<sup>37</sup> Solingen argues that state agencies and societal actors together may undertake joint projects or policy goals. According to Solingen, a grand strategy defines both a “country’s relationship to global power and economic structures” as well as “the internal extraction and allocation of resources among groups and institutions.”<sup>38</sup>

Solingen argues that there are two ideal type of ruling coalitions: internationalist-liberalizing and statist-nationalist-confessional. Internationalist-liberalizing coalitions are built of actors from competitive, “tradable” sectors which stand to gain from the opening of markets, those who would benefit from the distributional consequences of internationalization. Solingen argues that these coalitions quite often require insulation from some social forces and institutional capacity to succeed. These coalitions in general adopt positions of regional cooperation, which have several reinforcing consequences for the strength of the coalition: such a position can free up resources to carry out reform; secure access to foreign markets, capital, investment and technology; and weaken groups and institutions opposed to reform. Internationalist-liberalizing coalitions advocate engagement with international markets and structures, and an opening of the domestic economy to the world. A group of states dominated by these coalitions are likely to establish a cooperative regional order.

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<sup>37</sup> Etel Solingen, *Regional Orders at Century’s Dawn: Global and Domestic Influences on Grand Strategy* (Princeton: Princeton University Press, 1998), p. 9.

<sup>38</sup> *Ibid.*, p. 8.

Their antithesis, statist-nationalist-confessional coalitions, are composed of groups opposed to internationalization: sectors vulnerable to the opening of the domestic economy and introduction of market forces; state bureaucracies and politicians whose power is based in state control of the economy; and nationalist groups in conflict with neighboring nations. These coalitions tend to be inward-looking, preferring a larger role for the state in the economy and protection of the status quo. A constellation of states dominated by these coalitions generally produces a highly conflictual regional order. When no single type of coalition dominates consistently, one of three scenarios emerges: there is an oscillation of power between coalition types, a division of the state between coalitions, or a dissolution of the state altogether. Under any of these scenarios, neither an internationalist nor statist grand strategy can be implemented coherently and consistently.<sup>39</sup>

Solingen argues that coalitional strength and policy outcomes depend on the internal cohesiveness of and amount of political resources amassed by a coalition relative to its opposition. Contributing to these are the degree of macropolitical consensus in society, the amount of compensative resources the coalition possesses to distribute, the breadth of its support, etc. Solingen argues that, of the many cleavages in society and among social groups, the economic cleavages are the defining ones, and nationalism and confessional factors play a secondary role.

Solingen's argument contributes substantially to a solid basis from which to analyze the post-Soviet states. Her two broad categories of liberalizing and statist

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<sup>39</sup> Ibid., p. 53-54.

coalitions hold well for our cases, as does Solingen's scenario for the absence of a single dominant coalition. Her argument that the regional context provides incentives and opportunities around which social forces may coalesce is also consistent with the European NIS context. While Solingen's analysis is specifically targeted at East Asia, the Middle East, and Latin America, she does briefly address the question of the post-Soviet countries. Solingen argues that because they are more susceptible to populist forces<sup>40</sup> and reforms have often favored a concentration of wealth and widespread impoverishment,<sup>41</sup> the NIS are more likely to have weak internationalist and strong statist coalitions. It is important, however, to expand this analysis in order to account for the variation among ruling coalitions in the post-Soviet context.

There are several aspects of the European NIS cases that give rise to the need to elaborate on Solingen's framework. First, Solingen's two categories of coalitions, internationalist-liberalizing and statist-nationalist-confessional, must be unbundled. Solingen acknowledges that these are ideal-types, and that actual coalitions will rarely fit the ideal types precisely. Particularities of the post-Soviet context give rise to important variations from these types for several reasons. The policy choices before these states are not between internationalization and continued isolation *per se*. The highly-integrated economy of the Soviet Union left the NIS with the inheritance of highly trade-dependent economies, already "internationalized" in a sense from the very beginning of independence. Thus, the question facing policy-makers was not "internationalist" vs. "isolationist" (particularly in the arena of energy policy, in which no European NIS could

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<sup>40</sup> Ibid., pp. 105-107.

hope for autarky in the foreseeable future), but rather “globalist” vs. “Russophile”. The questions of liberalization vs. statism, of reform vs. status quo in the European NIS cases, however, do fit with Solingen’s ideal types.

Secondly, Solingen finds that internationalist-liberalizing coalitions tend not to align with nationalist movements, while statist groups provide natural coalitions partners for nationalist/confessional groups because of their conflict and rivalry with neighboring/competing nations or religions in the region. In the post-Soviet context, however, we find that opposite is often true for both practical and ideological reasons. The ideology and symbols of the Soviet era were at least nominally pan-nationalist. The state of the Soviet Union was an empire composed of many nations, which promoted the identity of the individual as a Soviet citizen above all other affiliations. In addition to this, the Soviet policy of settling ethnic Russian emigrants in the frontiers of the Union during the process of industrialization often produced regions within the now-independent republics most closely “nationally” affiliated with Russia, as well as most economically tied to Russia. The symbols of the pre-Soviet nation and religion were most easily adopted and widely recognized in the battle to reject the Soviet mantle. In the struggle for independence, globalist market liberalizers often became easy allies with nationalists and religious revivalists through their shared opposition to Soviet statist-socialist economic policy and repression of national identity and religion. Ironically, those in statist coalitions often advocated the most inclusive, pan-national or cosmopolitan definitions of the new nation.

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<sup>41</sup> Ibid., p. 51.

I will argue that a state-in-society approach to domestic coalition formation is the key to explaining energy policy in the former Soviet Union. Political coalitions have risen from the dust of the old ministries and Soviet diasporas not only to defend their existing stakes in the fuel industry, but to wage battle over control of the state and the future of the country itself. These battles are many-faceted, and are awkwardly conceptualized in terms of the current discipline. These battles are the stuff of domestic politics insofar as nominally private actors compete with one another and lobby the state for assistance. They are traditional international relations to the extent that these states bargain amongst themselves for access to resources that enhance their security. And they are also something more akin to international political economy, when private domestic actors interact with foreign private actors and even foreign states. It is not that we cannot categorize the various competitions and interactions in terms of each approach. It is rather that by categorizing these competitions this way, thus in effect treating them as separate and unrelated phenomena, we lose the opportunity to understand their interrelations and similarities. I propose to examine these phenomena through the lens of a state-in-society approach, building on the ideas of Migdal, Shue, Chaudhry and Solingen on materialist-ideational coalitions and Solingen's arguments on regional context and the international orientation of domestic political coalitions.

#### **V. A State-in-Society Approach to Domestic Coalitions: The Political Costs of Energy Reorientation**

I will argue that seemingly "weak" states can act autonomously when they have the support of well-organized social groups and are able to pass the costs of their policies

onto less-organized or divided social groups. In the cases of the European NIS and energy trade reorientation, this meant that states dominated by globalist-liberalizing-nationalist coalitions were able both to choose strategies of energy trade reorientation and to implement those policies successfully by politically disenfranchising the ethnic minorities who populated the economically most vulnerable sectors. These were Estonia and Latvia, the “globalizers”. As Migdal and Solingen argue, however, state priorities cannot simply be assumed, and we cannot assert that any state with a degree of insulation or “autonomy” would choose globalization. We must first examine the interests of those social groups allied with the states. Unlike those of the globalizers, the state of Belarus, which was dominated by pro-Moscow-statist-leftist coalitions, used its capacity to successfully pursue the opposite strategy: it embraced its energy dependence on Moscow and sought to preserve its energy subsidies. Belarus was the “Russophile”.

Still a third variant emerged: states which were themselves fragmented, divided against themselves between coalitions allied with liberalizing social groups and those allied with statist groups, or states which changed hands between globalist-liberalizing and pro-Moscow-statist coalitions. Just as Solingen predicts, these states failed to implement either sort of policy consistently, producing troubled, hybrid economies and continued energy dependence on Russia. These were Lithuania, Moldova, and Ukraine, the “hybrids.” The hybrid may come to be dominated by groups which benefit from the rent opportunities generated by a mixed economy ensuring a hybrid strategy for some time to come.

Analytical parallels between Chaudhry's cases and those of the European NIS -- specifically between that of the successful reformer, Yemen, and the cases of successful reform in the NIS, Latvia and Estonia -- can inform our understanding of the role of social groups in economic reform. Just as the Yemeni state was able to implement difficult economic reforms because of its separation from private business interests and the ethnic group which dominated them, the disconnect in Latvia and Estonia between the state and the heavily-industrialized, Russophone minorities facilitated the implementation of energy trade reorientation (and the sectoral restructuring that necessitated) by the state. In our cases, multiple conceptions of "national" identity vied for predominance and for partnering with the materially-defined social forces for political domination. Like identity-based groups in Chaudhry's cases, the boundaries and definitions of these groups were influenced by materially-based interests.

There often exists both in international political economy and comparative politics a division between theorists who see institutions as the independent variable and those who see coalitions or sectors as the independent variable. I see coalitions and institutions as interrelated. Domestic political institutions constrain coalitions and shape the strategies and leverage available to them. For example, in representative democracies, is it not only the industrial interests but also consumers and labor who may effectively organize to pressure the state. In states with more authoritarian structures, industrial supporters may indeed have access to the corridors of power, while labor and consumers may be denied any institutionalized access to policy-makers.

However, in the cases being investigated here, the states at the advent of independence possessed Soviet-style institutions which were very similar to one another. The post-Soviet context may be as close as we political scientists can come to “controlling” for institutional variance. Thus, in these cases, the independent impact and constraints of domestic institutions should be very similar, and their significance in the explanation of the differences in trade and policy outcomes minimal. Certainly many of these institutions have been altered since the states became independent. This is not the product of some natural evolution toward modernization, but rather the result of political contests and agreements among coalitions. Domestic coalition formation, therefore, is our central explanatory variable.

Table 1.1 Summary of Cases: Political Coalitions and Energy Strategy

Consensus coalition: pro-market and pro- West			Globalizers: Estonia Latvia
Lack of consensus: fragmentation or oscillation of power		Hybrids: Lithuania Moldova Ukraine	
Consensus coalition: socialists and pro- Moscow	Russophile: Belarus		
	No decline in import dependence or share of imports from Russia. No strategic balancing investment.	Moderate to low decline in import dependence and share from Russia. Low strategic balancing investment.	Decline in import dependence and share of imports from Russia. High strategic balancing investment.

I examine the political costs of economic restructuring and energy reorientation. The economic costs of restructuring would be high for all cases. The political costs, however, differ. The presence of a politically “excludable” group, onto which the costs of energy trade reorientation might be thrust, is a facilitating condition for such restructuring. Domination of the state by a pro-internationalist coalition is the important condition. I argue that:

- Governments will implement policies of energy reorientation, economic restructuring, and engagement with the global economy where the economic costs of doing so are borne disproportionately by relatively poorly-organized, divided, politically disenfranchised groups, as in the cases of Estonia and Latvia. Both the conditions are present. This produces a globalizer outcome.
- Conversely, when energy subsidies are highly important to powerful groups allied closely with the state, as in the case of Belarus, the government will avoid energy reorientation and restructuring and seek protection from global competition. Neither condition is present. This leads to the Russophile strategy.
- Where the costs of energy reorientation would be borne by large but diffuse social groups, governments cannot maintain consensus, producing oscillation in power and policy and slower progress toward diversification of energy suppliers and economic restructuring, as in the cases of Lithuania, Moldova and Ukraine. One condition may be present, but not both. This produces a hybrid strategy, which may emerge as a politically sustainable (though economically suboptimal) outcome.

## **VI. Summary**

I propose to examine the cases of the European states that were formerly members of the Soviet Union, that is, Ukraine, Belarus, Moldova, Latvia, Lithuania and Estonia.

This case selection is based on a most-similar-systems logic.<sup>42</sup> Isolating the universe of cases to a particular region to some extent controls for large differences in access to world markets: states sandwiched between Russia and China face very different opportunities and constraints from those seated between Russia and the European Union. Choosing the European group of former Soviet states over those, for instance, in the Caucasus or Central Asia eliminates those states that could quite easily attain energy autarky or even become net exporters, such as Azerbaijan and Kazakhstan. Because the question at hand focuses on energy dependence and trade, states which are historically and presently net energy importers make better case studies.

Many of the Soviet satellite states of Eastern Europe, while not formally part of the Soviet Union, were also dependent upon the Soviets for energy. They have not been included as case studies in this project because NIS shared more similar Leninist and Stalinist institutional structures that help to control for a greater number of potential variables. While it is true that their political systems often were very similar to that of the Soviet Union, and that their politics were certainly influenced (if not completely orchestrated) by Moscow, the fact of their formal sovereignty and independence during the Soviet era, their informal divergences from strict Leninism, geographical differences, and radically different history of independence might prove confounding variables.

I argue that where the high costs of restructuring are borne by a politically disenfranchised group, a consensus coalition can emerge in favor of rapid restructuring and energy reorientation. Where the high costs of restructuring are borne by powerful

interest groups close to the state, a coalition emerges in favor of maintenance of energy subsidies from and political relationship with Russia. Where the costs of restructuring are borne broadly or by highly organized groups, compromise governments will make slow or little progress toward energy reorientation and reform. In the cases of the European successor states to the Soviet Union, energy trade is at the heart of this restructuring, both in terms of defining domestic economic coalitions and in terms of opportunities and constraints on relations with Russia.

In the globalizers, Estonia and Latvia, strongly pro-Western, pro-market coalitions restructure the domestic economy and international energy trade toward the global economy. These states bear the short-term costs of restructuring in favor of long-term economic growth, greater autonomy from Russia and greater integration into Western Europe. In the Russophile case, Belarus, a strongly pro-Russian, anti-market coalition maintained the basic structure of the domestic economy and energy trade dependency on Russia. It avoided some of the immediate costs of restructuring, and hoped to bolster its faltering economy through further integration with and subsidization by Russia. Where such dominant coalitions are absent, mixed policies emerge. In Lithuania, an inclusive nationalism and oscillation between reformist and communist parties produced a contraction in energy imports from Russia but little energy reorientation, and did not lead to the significant domestic economic reforms necessary to a strong, independent economy. In Moldova and Ukraine, the quick demise of nationalist/reformist parties in favor of pro-Russian, anti-reform coalitions, and the

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<sup>42</sup> Adam Przeworski and Henry Teune, *The Logic of Comparative Social Inquiry* (New York, Wiley-

subsequent battles between these fragmented forces and between competing nationalities, prevented single coalitions from dominating. These states continued to depend on Russia for discounted energy supplies, while intermittently attempting reform and trade reorientation.

The second chapter of this study outlines Russia's foreign and energy trade policies in the transition period. Russia's interest in maintaining control, or at least influence, in the "near abroad" drove it to keep the door open to continued subsidization of all the NIS in this study. It was up to the NIS themselves to close that door, or to walk through. Chapter three outlines the broader theoretical findings and statistical data across all six cases. Chapter four is a detailed account of the case of Estonia, as well as a brief summary of the other globalizer, Latvia. Chapter five focuses on the hybrids and includes an examination of the Lithuanian case as well as summaries of the Moldovan and Ukrainian cases. Chapter six explores the case of the Russophile, Belarus. Chapter seven discusses the implications of this study for our understanding of post-socialist transitions and the process of globalization, as well as the future prospects for the European NIS.

## CHAPTER II

### RUSSIA AND THE STEEL UMBILICAL CORD<sup>1</sup>

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#### I. Introduction

On March 11, 1990, the Lithuanian Supreme Council declared full independence from the Soviet Union and elected Vytautas Landsbergis head of state. A week and a half later, the Soviet army apprehended Lithuanian deserters in Lithuania and began to seize former Communist Party buildings in Vilnius. These military actions only increased the morale and determination of the independence movement, leading to popular demonstrations.<sup>2</sup> On April 19th, however, Moscow suspended all shipments of oil and most gas to Lithuania, effecting an energy embargo of the country. The fuel embargo began to take its toll on Lithuania, threatening to lead to a poor harvest and severe food shortages. Finally, on June 28th, the Lithuanian Supreme Council acquiesced and accepted a moratorium on the declaration of independence, beginning negotiations with Moscow. The fuel blockade was lifted.<sup>3</sup>

This incident was not the first time Moscow used fuel supply as a political tool, nor the last. Russia's relations with Eastern Europe and the Near Abroad were in large part shaped by these countries' energy dependence upon the Soviet Union, and upon

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<sup>1</sup> Robert Ebel coined this apt phrase to describe the infrastructure of fuel pipelines flowing from Russia to the resource-poor members of the Soviet Union, feeding them heavily subsidized oil and natural gas. *Energy Choices in the Near Abroad: The Haves and Have-Nots Face the Future* (Washington, D.C.: Center for Strategic and International Studies, 1997).

<sup>2</sup> Anatol Lieven, *The Baltic Revolution: Estonia, Latvia, Lithuania and the Path to Independence* (New Haven, CT: Yale University Press, 1993), p. 239.

Russia specifically. Moscow's use of energy trade as a tool of high politics persisted after the demise of the Soviet Union. Russia inherited the lion's share of Soviet energy resources and infrastructure, and continued to use the supply of fuel, discounted prices and tolerance of nonpayments as incentives to would-be allies in the former Soviet Union long after that Union was no more. Russia attempted to use these fuel embargoes and subsidies as inducements to NIS to join the Commonwealth of Independent States, to persuade the NIS to sign economic and security agreements with Russia, and to pressure the NIS into adopting friendlier policies toward the Russian diaspora. While membership in the CIS and access to cheap Russian energy were available to all, including the Baltic states, they were not without cost. Belarus chose to embrace fully this relationship with Russia. Estonia and Latvia rejected it. Others, such as Lithuania, Moldova and Ukraine, adopted hybrid strategies.

Russian foreign policy toward the "near abroad" centered around a number of issues stemming from the dissolution of the empire: the definition of the borders of the new Russian sphere of influence; the degree of responsibility of Russia to play the role of peacekeeper in this region; Russia's role in protecting the rights of the Russian diaspora; the status of the CIS as new Soviet Union or merely a loose confederation of states; and collective security among the NIS. Interrelated with these issues were several concrete problems, including the questions of troop withdrawals, citizenship rights, and economic relations. The question of ownership of the Black Sea fleet and the status of Crimea proved a nettle in Russian-Ukrainian relations. Nuclear disarmament of Ukraine and

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<sup>3</sup> Lithuania did ultimately secede, despite the blockades and intervention, and was finally recognized

Belarus dominated relations for a time. The issue of access to Kaliningrad, the Russian exclave on the Baltic Sea most easily accessible through crossing the territory of Lithuania, raised difficulties for the two states particularly in terms of transportation and troop movements. The new borders which resulted from the dissolution of the Soviet Union robbed Russia of access to many of the ports essential to commerce, particularly those in Latvia and Ukraine. Interwoven with these issues, used alternately by Russia as a carrot and a stick to leverage Russia's position, was the issue of energy supply. Russia needed access to Western markets through at least some of the European NIS. All of the European NIS needed energy imports, and subsidized energy imports if they were to maintain the current composition of their economies.

To be sure, political groups within Russia viewed the post-Soviet world, and Russia's role in it, very differently. The "neo-liberals" such as Egor Gaidar and Andrey Kozyrev, who gained positions of power when Yeltsin was elected in 1990, advocated a non-expansionist role for Russia and equal status among the NIS, supporting Ukraine's view of the CIS as a tool of an "amicable divorce." Nationalists, such as then-Vice President Aleksander Rutskoy and then-Supreme Soviet Chairman Ruslan Khasbulatov, strongly advocated reintegration of the non-Russian states within the CIS, and the use of the CIS itself as a tool for maintaining the Russian empire. They advocated, and at times executed, a highly interventionist stance by Russia in the "near-abroad" in order to reassert Russia's Great Power status. The conflict between the two sides came to a head in 1993 in the confrontation between Yeltsin and the Russian parliament. While this

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by Moscow over a year later, in September 1991, helping to spark the eventual dissolution of the USSR.

resulted in the ouster of these particular nationalists, the Russian people elected to the new parliament an array of neo-communists and nationalists, and Yeltsin was eventually forced to compromise in foreign policy matters with these groups. Activist Russian “peacekeeping” became an important facet of official Russian foreign policy, as well as the promotion of the CIS as a supranational organization, with Russia playing a role somewhat “more equal” than the others. While there remained division on these foreign relations questions, with neo-liberal forces advocating a limited role for Russia in the near abroad and extreme nationalists such as Vladimir Zhirinovskiy advocating radical expansionism, the middle-course pursued by the Russian state was one of attempting to maintain the Russian sphere of influence through economic subsidies, institutional integration, and limited military intervention.<sup>4</sup>

This chapter outlines the opportunities and constraints posed to the NIS by Russian foreign and energy trade policy, and the context within which the NIS made their policy choices regarding post-Soviet relations with Moscow. Part II describes a brief history of the politics of Soviet energy trade and subsidies. Part III outlines the role of the Commonwealth of Independent States in post-Soviet energy politics. Part IV provides an account of Russian policies of energy pricing and embargoes toward the NIS. In the conclusion I discuss the future, and the possible folly, of this reliance on Russian energy subsidies.

## II. Soviet Subsidization: Developing Dependencies

### *Energy as bargaining chip*

The Soviet Union used the promise of cheap energy to Eastern Europe as a central bargaining chip in alliance politics and policy compliance. But perhaps the politics of Soviet energy trade are best known in the context of Cold War-era exports to the West. Bruce Jentleson<sup>5</sup> describes the inherent political and security implications of this economic relationship. From the beginning of the Cold War, the United States was wary of energy trade with the Soviet Union. United States policy makers were concerned not only that the sale of Soviet oil and natural gas would increase Soviet hard-currency earnings, providing fuel for technological and military advancement, but also that the United States' European allies would become too dependent on Soviet energy imports.

The US policy of economic coercion, that is, trade restrictions against the Soviet Union, gave way to economic inducement in the 1970s détente era. Trade controls, specifically in the energy and grain sectors, were liberalized in an effort to elicit political cooperation from the Soviet Union. Domestic political resistance to this strategy and its failure to restrain Soviet intervention in the Third World hastened its demise, and US policy subsequently oscillated between promoting and restricting energy trade with the Soviet Union. It must be noted that the trade policy in this area was not driven merely by economic concerns, or "low politics." Quite the contrary: energy trade policy with the

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<sup>4</sup> Zbigniew Brzezinski and Paige Sullivan, eds., *Russia and the Commonwealth of Independent States: Documents, Data and Analysis* (Armonk, N.Y.: M. E. Sharpe, 1997).

<sup>5</sup> Bruce W. Jentleson, *Pipeline Politics: The Complex Political Economy of East-West Energy Trade* (Ithaca, N.Y.: Cornell University Press, 1986).

Soviet Union was a tool and reflection of security concerns, of strategic political objectives, that is, of “high politics.”

William Reisinger, in *Energy and the Soviet Bloc: Alliance Politics after Stalin*, outlines the political implications of energy dependence within the Soviet Bloc. Reisinger argues that deeply discounted oil and natural gas were supplied to Soviet allies in Eastern Europe when these allies cooperated in defense matters with the Soviet Union, and were withheld when the Eastern European allies fell out of favor. These discounted energy exports amounted to implicit subsidies of the Eastern European economies, particularly when world market prices climbed. Reisinger tests a variety of nonpolitical factors as explanations for which Eastern European states benefited from favorable Russian energy export prices, but finds Soviet political and security concerns to be the best and most consistent explanations of these patterns:

The subsidies were not uniform across countries... [D]ifferences across the East European states with regard to the quantity and price of various types of fuel are noticeable and cannot be well explained by nonpolitical factors. The division between the favored and nonfavored states corresponds to the closeness of these states' policies, in several areas, to Soviet desires.<sup>6</sup>

Reisinger finds that the magnitude of subsidies differed widely. For example, the subsidy received by the German Democratic Republic in 1978 was 16.5 times as high as that received by Romania. By the early 1970s, it was clear that the Soviet Union gave markedly higher fuel subsidies to the GDR, Bulgaria and Czechoslovakia than to Hungary, Poland or Romania, because the former countries' political and security policies more closely complied with Soviet wishes.

*The Soviet energy system*

The supply of energy was an important policy tool for the Soviet Union not only in its international relations, but also in its domestic politics. The underpricing of Soviet energy, and the inefficiency<sup>7</sup> it spawned, had two origins. The first was the nature of the state-owned economy itself. Thane Gustafson, in *Crisis amid Plenty: The Politics of Energy under Brezhnev and Gorbachev*, argues that command economies generate informational problems, with pricing systems that yield false signals about supply, demand and efficiency. Such systems also produce irrational incentives and distorted rewards.<sup>8</sup> The Soviet command economy was characterized by overinvestment in the energy sector, overuse and underpricing of energy.<sup>9</sup> In addition to these structural distortions, the underpricing of energy was also driven by political factors. The Soviet Union's economic system was built around the goal of rapid industrialization, especially the promotion of heavy industry. Undervaluing the cost of energy inputs facilitated the achievement of this goal.

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<sup>6</sup> William M. Reisinger. *Energy and the Soviet Bloc: Alliance Politics after Stalin* (Ithaca, N.Y.: Cornell University Press, 1992), p. 81.

<sup>7</sup> Many Soviet enterprises were inefficient in their use of resources or even had a negative value-added when industrial inputs such as energy and raw materials were calculated at world-market prices.

<sup>8</sup> Thane Gustafson. *Crisis amid Plenty: The Politics of Soviet Energy under Brezhnev and Gorbachev* (Princeton, N.J.: Princeton University Press, 1989), p. 10.

<sup>9</sup> For example, Ed Hewett finds that, even at over-inflated official Soviet exchange rates, the 1981 enterprise wholesale price of crude was \$4.62 (3 rubles) per barrel, compared with the world market price at the time of \$33 per barrel. Underpricing of energy was endemic to the Soviet planning system. Ed A. Hewett, *Energy, Economics and Foreign Policy in the Soviet Union* (Washington, D.C.: Brookings Institution, 1984), p. 135.

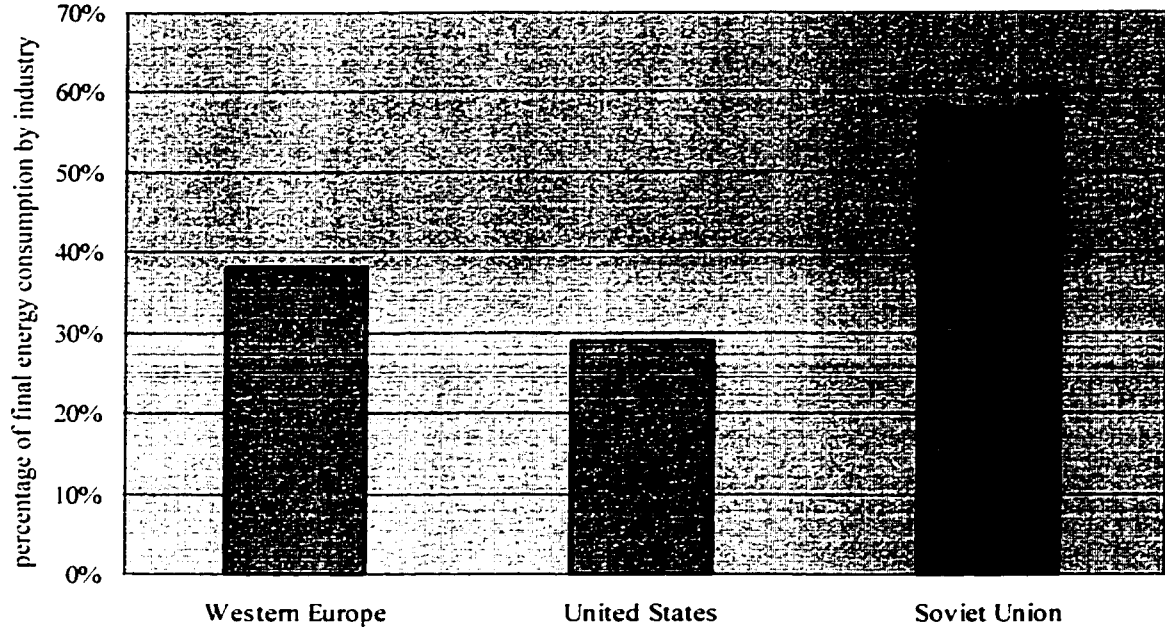


Figure 2.1. Percentage of Total Final Energy Consumption by Industry, 1980

Source: Ed A. Hewett, *Energy, Economics and Foreign Policy in the Soviet Union* (Washington, D.C.: Brookings Institution, 1984), p. 107.

Gustafson argues that industry was one of the major obstacles to increasing efficiency in Soviet-built economies. Industry accounted for a far greater share of energy consumption in the Soviet economies than it did in other major industrial countries (see figure 2.1). Gustafson argues that this bodes ill for the prospects of increasing the energy-efficiency of the economy, as “industrial consumption is more difficult, expensive and time-consuming to alter than transportation or residential consumption,”<sup>10</sup> which hold a larger share of energy consumption in other industrialized economies. In addition,

<sup>10</sup> Thane Gustafson, *Crisis amid Plenty: The Politics of Soviet Energy under Brezhnev and Gorbachev* (Princeton, N.J.: Princeton University Press, 1989), p. 232.

Soviet-built industry is a less efficient energy consumer. As an illustration, in 1980, Soviet industry consumed 56% more energy per unit value added than did US industry.<sup>11</sup>

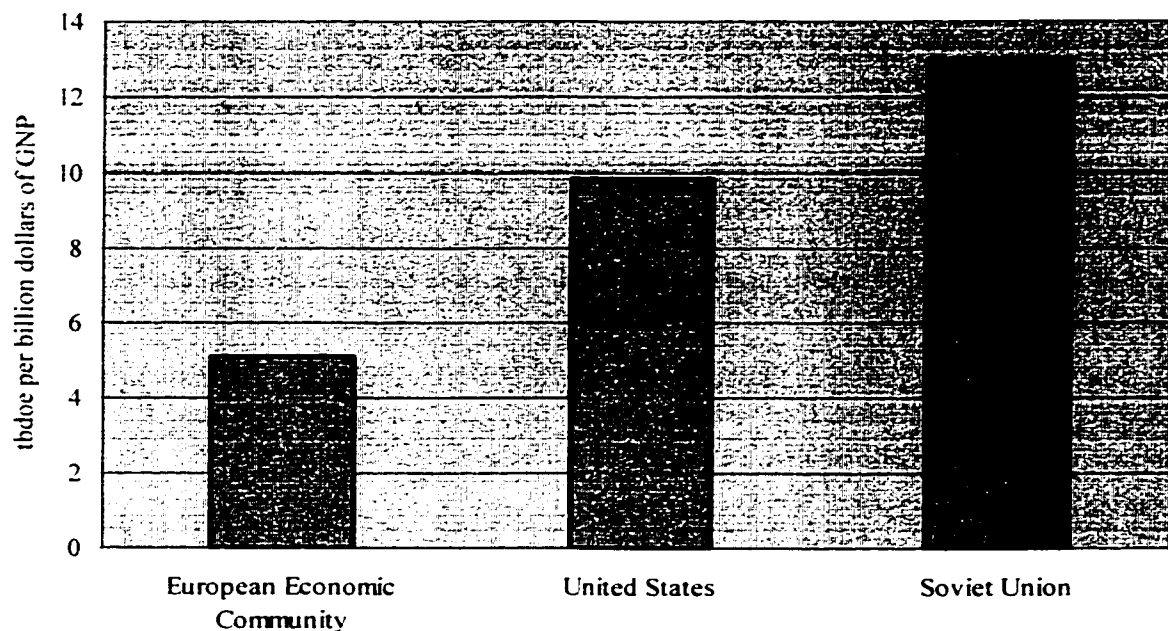


Figure 2.2. Comparative Energy Intensity of Selected Industrialized Economies: Energy Consumption per Unit of GNP, 1980

Source: Ed A. Hewett, *Energy, Economics and Foreign Policy in the Soviet Union* (Washington, D.C.: Brookings Institution, 1984), p. 105.

Soviet industry was concentrated in energy-intensive sectors (such as heavy industry and metallurgy), made wasteful use of the end products of these industries (thus driving demand and energy consumption still higher), and was wasteful of energy in its industrial

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<sup>11</sup> Ibid., p. 233.

processes.<sup>12</sup> This produced an economic system which consumed an inordinate amount of energy per unit of production value (see Figure 2.2). It was this economic system that the NIS inherited upon independence.

Soviet development of the energy sector also ensured that the costs of a potential break-up would be very high: the development of Russian energy resources over those of the other republics and the routing of the production of these republics through Russia produced a deep and abiding energy interdependence among the Soviet republics. No states (with the exception of Russia herself), even those with substantial indigenous energy reserves, would be immediately energy self-sufficient. Those without energy resources of their own were completely and profoundly dependent upon supply from Russia.<sup>13</sup>

*The end of empire: the "domestic" becomes "international"*

At the end of 1991, the Soviet Union came to an end. Political and economic relations between Russia and the "near abroad" were no longer domestic matters determined by central planners in Moscow, but rather issues to be negotiated between the former ruler and the newly independent states. This is not to say that the economic structure of the region was instantly transformed, however: the industries which had been built on virtually free energy still required inordinate amounts of it in order to operate. Furthermore, the introduction of market forces put pressure on many of these industries to

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<sup>12</sup> Ibid., p. 233.

<sup>13</sup> Robert Ebel, *Energy Choices in the Near Abroad: The Haves and Have-Nots Face the Future* (Washington, D.C.: Center for Strategic and International Studies, 1997).

produce goods that were competitive at world-market prices. If energy inputs were no longer free, but rather purchased at world-market prices as well, many of these factories and industries would produce products which, in the end, were worth less than the sum of their inputs. They would either need to maintain subsidies from the state or to close down. This posed difficult policy dilemmas to the leaders of the NIS: to attempt to maintain access to cheap Russian energy in order to sustain inefficient domestic industry, at the cost of remaining within Russia's sphere of influence, or to sever the relationship, suffering industrial closures and unemployment, but gaining access to global market and Western political alliances.

In the meanwhile, Russia inherited from the Soviet collapse immense energy resources and infrastructure. Russia found itself in possession of the vast natural gas fields of West Siberia, the northwestern Komi region, the Volga-Ural and North Caucasus regions of the Russian southwest, in addition to prospective production in East Siberia, the Lena-Tungusha region, the waters off of Sakhalin Island in the Far East and the Caspian Sea to the south. Russian oil resources included reserves in the Timan-Pechora and Barents Sea areas, West Siberia, the Volga-Ural and North Caucasus regions. Untapped potential in this sector seemed even more substantial, with vast estimated reserves in East and West Siberia, the Russian Far East, the North Caspian, and the Seas of Okotsk, Chukchi, East Siberia, Laptev, and Kara. Russia now possessed some of the largest oil reserves in the world and *the* largest reserves of natural gas on the planet. Six of the world's ten top-producing gas fields belonged to Russia. In addition to these resources, the legacy of the Soviet energy infrastructure favored Russia: the export

pipelines from the handful of other post-Soviet states to inherit their own substantial energy resources (Azerbaijan, Kazakstan, Turkmenistan and Uzbekistan) by and large ran through Russian territory. This gave Russia great control over their resources as well. In addition, import pipelines to the energy-poor states (the remaining ten NIS) radiated out from Russia, transforming, after the fall, their dependence on the Soviet Union into dependence on Russia.

### **III. Russian Realpolitik: CIS and Foreign Policy toward the NIS**

#### *The Commonwealth of Independent States*

In 1991, Moscow saw the Soviet Union dissolving around it. Latvia, Lithuania and Estonia, following the failed coup in August,<sup>14</sup> announced their independence. While Gorbachev struggled to hold onto power, official recognition of Baltic independence by Western nations came in September.<sup>15</sup> In August, President Yeltsin of Russia recognized the independence of the Baltic states in his own bid against Gorbachev to secure “independence” for Russia and status as head of state for himself. On December 1<sup>st</sup>, 1991, voters in Ukraine overwhelmingly cast their ballots in favor of independence from Russia. On December 8<sup>th</sup>, 1991 the leaders of Belarus, Ukraine and Russia met in the Belarusian forest to declare their secession from the Soviet Union, its *de facto* dissolution, and to establish a new association among the republics. The Minsk Treaty, the founding document of the Commonwealth of Independent States, was signed. The

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<sup>14</sup> “Breakup of the Soviet Union: It’s Official: Independence for the Baltics” *Los Angeles Times* September 7, 1991. Online. LEXIS-NEXIS Academic Universe.

signatories invited other NIS to sign, and declared the Commonwealth of Independent States open to all members of the former Soviet Union.<sup>16</sup>

The Minsk meeting was followed only weeks later by a gathering in Alma Ata of the leaders of most of the other members of the former Soviet Union. The treaty signed there officially dissolved the Soviet Union, replacing it with the CIS, which was to coordinate defense, foreign affairs and economic policy.<sup>17</sup> Perhaps most important to the attendees, the treaty imparted to the states de facto independence, and transformed the leaders from regional governors into heads of sovereign states. Eleven of the fifteen members of the former Soviet Union signed the Alma Ata treaty, though it was open to all, including the Baltic states.<sup>18</sup> Both Ukrainian President Leonid Kravchuk<sup>19</sup> and Russian President Boris Yeltsin<sup>20</sup> explicitly invited Latvia, Lithuania and Estonia to join the Commonwealth. However, these three states, having already gained independence and international recognition prior to the gathering of the NIS, roundly dismissed<sup>21</sup> the possibility of joining the CIS, and declined even to attend the meeting at Alma Ata.

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<sup>15</sup> Trei, Lisa, Igor Reichlin and Stewart Toy. "Balts are Free – But 'Winter is Coming'" *Business Week* September 9, 1991. Online. LEXIS-NEXIS Academic Universe.

<sup>16</sup> "Declaring Death of Soviet Union, Russia and 2 Republics Form New Commonwealth" *New York Times* December 9, 1991. Online. LEXIS-NEXIS Academic Universe.

<sup>17</sup> Nadler, Gerald. "Soviet Union is Laid to Rest: Republics form Commonwealth of Independent States" *Washington Times* December 22, 1991. Online. LEXIS-NEXIS Academic Universe.

<sup>18</sup> A representative from the fifteenth republic, Georgia, attended the Alma Ata meeting but declined to sign the treaty. Russia later pressured Georgia into acquiescing to CIS membership.

<sup>19</sup> "Other Soviet Republics Ponder New Slavic Commonwealth" *United Press International* December 11, 1991. Online. LEXIS-NEXIS Academic Universe.

<sup>20</sup> "Commonwealth Open to Balts, Yeltsin Says" *Agence France Presse* (France) December 12, 1991. Online. LEXIS-NEXIS Academic Universe.

<sup>21</sup> "Estonia: Estonian Premier Says Commonwealth Has No Future" *British Broadcasting Corporation* December 14, 1991, and "Balts Won't Join Soviet Commonwealth: Latvian Foreign Minister" *Agence France Presse* (France) December 12, 1991. Online. LEXIS-NEXIS Academic Universe.

Membership in the Commonwealth of Independent States correlates with the maintenance of energy subsidies: our Russophile and two of the three hybrids belong to the CIS. However, one must examine not only membership in the CIS, but also bilateral relations, in order to explain energy trade policy between the various NIS and Russia. The evidence indicates that while NIS predisposed to favor continued ties with Russia may have chosen to join the CIS, CIS members did not receive the same magnitude or reliability in energy price subsidies. Indeed, non-CIS hybrid Lithuania in some cases secured the same level of subsidies as CIS members. Furthermore, some CIS members may pay *more* than non-CIS members for certain energy inputs. The CIS is a good, though imperfect, indication of the foreign policy orientation of the NIS.

Russian policy toward the CIS developed over time. In the beginning, the CIS was a means by which Yeltsin could wrest control of Russia from Gorbachev. It was also a tool with which Russia hoped to accomplish two broad policy goals: to preserve the ruble zone, and to preserve Russia's influence in the "near abroad." In 1992, immediately after the founding of the Commonwealth of Independent States, Russia's policy toward the NIS and CIS was somewhat muddled, as conflicts over foreign policy priorities between the president and parliament raged, and as the Russian domestic economic crisis took policy priority.

However, in 1993, a clearer foreign policy focus in Russia began to emerge.<sup>22</sup> Russia perceived the greatest threat in the NIS to be from regional armed conflicts and from political and economic reorientation of the NIS to outside powers, particularly

Europe. Russia saw power in the NIS as essential to the preservation of its “great power” status, and actively promoted ties with the NIS. Russia promoted integration via the CIS and bilateral treaties with the NIS. It “reorganized” and legitimated the presence of its troops in many of the NIS rather than withdrawing them, and played an active role in “peacekeeping” in the regional armed conflicts in the NIS. Russia’s stated objectives in the NIS were to obtain strategic control of the territories of the former Soviet Union and to deny a strategic presence in the NIS to other world powers. In September 1995, Russia issued an official document on the “near abroad”, stating that the CIS was a “zone of Russian interest.” and that the presence of other powers would not be tolerated.<sup>23</sup>

#### *CIS membership and the European NIS*

The NIS reacted to Russian policy in very different ways. Notably absent from the Alma Ata signatories were Latvia, Lithuania, Estonia and Georgia, who refused to participate in the new organization. Azerbaijan later withdrew from the CIS, much to Russia’s dismay. Russia managed to pressure Azerbaijan and Georgia to return to the fold, however. In exchange for Russia’s support of the Georgian regime against the armed Abkhazi insurgency (which Russia was secretly promoting), Georgia agreed to become a member of the CIS. In September 1993, Georgia signed the Tashkent Treaty on Collective Security, as well as an agreement to allow Russian military bases on Georgia

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<sup>22</sup> Birthe Hansen and Bertel Heurlin, eds., *The Baltic States in World Politics* (New York, N.Y.: St. Martin’s Press, 1998).

<sup>23</sup> *Ibid.*, p. 115.

territory. Azerbaijan rejoined the CIS also in 1993, after suffering through its own armed conflict in Nagorno-Karabakh, and signed the Tashkent Treaty as well.<sup>24</sup>

The Baltic States refused to be persuaded, however. Latvia, Lithuania and Estonia declined to participate in the CIS or any of its related treaties, despite fuel blockades, rising energy prices, and Russia's delaying of withdrawal of troops from Baltic territory. Ukraine and Moldova joined the CIS, though their enthusiasm for reintegration with Russia must be said to have been limited. Ukraine's use of the CIS has often been described as a tool for an "amicable divorce". While Ukraine was one of the founding members of the CIS, it often expressed opposition to integration with Russia<sup>25</sup> and repeatedly delayed ratification of CIS-related treaties.

Moldova acceded to the CIS under duress: conflict in the Trans-Dniester region was taking its toll, and the Russian 14<sup>th</sup> Army, along with a myriad of Russian nationalist adventurers, occupied its territory. Russia possessed considerable economic leverage over Moldova as well: while Moldova had signed the treaty at Alma Ata, it had failed to ratify it, putting its CIS membership on hold. Russia placed enormous excise and value-added taxes on agricultural imports for Moldova at the same time that it increased energy prices.<sup>26</sup> The resulting decline in Moldovan exports to Russia deprived it of the means by which to pay for Russian energy imports.<sup>27</sup> Under this pressure, Moldova ratified the CIS

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<sup>24</sup> Ibid., p. 114.

<sup>25</sup> Tom Casier and Katlijn Malfliet, eds., *Is Russia a European Power? The Position of Russia in a New Europe* (Leuven, Belgium: Leuven University Press, 1998), p. 96.

<sup>26</sup> Radio Free Europe/Radio Liberty, *Newsline* (November 5, 1993) "Moldova Damaged by Russian Economic Pressure."

<sup>27</sup> Radio Free Europe/Radio Liberty, *Newsline* (March 14, 1994) "Moldova Still Hurting from Russian Trade Restrictions."

treaty in 1994.<sup>28</sup> Russia and Moldova subsequently came to better terms on energy payments and deliveries.

Belarus was a far more enthusiastic member of the CIS. Belarus hosted the initial conference that led to the demise of the USSR and the creation of the CIS, and volunteered to serve as the capital of this body. Economic and political cooperation with the CIS was not enough for Belarus, however. Belarus pushed for still deeper integration with Russia on a bilateral basis.

#### *CIS membership and energy trade*

Membership in the CIS meant some serious policy compromises for the NIS. Russian troops continued to occupy their territories and to influence not only their foreign policies, but in some cases their domestic policies as well. There were also benefits to membership, however. Preferential trade policies with Russia maintained export markets for many of the poor-quality NIS goods that would have been difficult to sell on the world market. Perhaps more importantly, CIS states on average benefited from much lower prices on Russian goods and primary inputs, particularly energy (see Figures 2.3 and 2.4). For many NIS, the CIS was a means by which to sustain the fuel subsidies on which their economies were based.

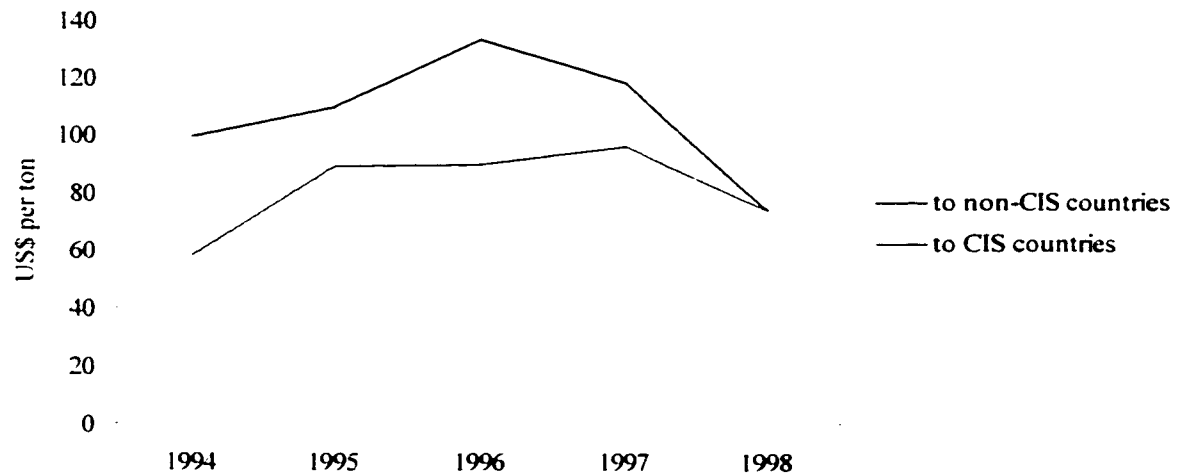


Figure 2.3 Average Price of Russian Exports, Crude Oil, 1994-1998

Source: State Ministry of Statistics of the Russian Federation, Special Report prepared for this study, October 1999. <sup>29</sup>

It is clear that CIS members generally enjoyed preferential pricing structures in terms of their energy inputs from Russia. However, CIS membership in itself was not enough to guarantee receipt of subsidies, nor to ensure their continuation. Energy discounts from Russia to various CIS members differ greatly, depending in large part on bilateral relations at the time. Subsidies to Moldova increased as Russia and Moldova reached accommodation on CIS membership and the Trans-Dniester issue. Subsidies to Ukraine declined as relations between Russia and Ukraine worsened. Energy subsidies to

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<sup>28</sup> Radio Free Europe/Radio Liberty, *Newsline* (April 11, 1994) "Moldovans Ratify CIS Membership, Economic Union."

Belarus remained high, even as the difference between average CIS prices and non-CIS prices began to converge.

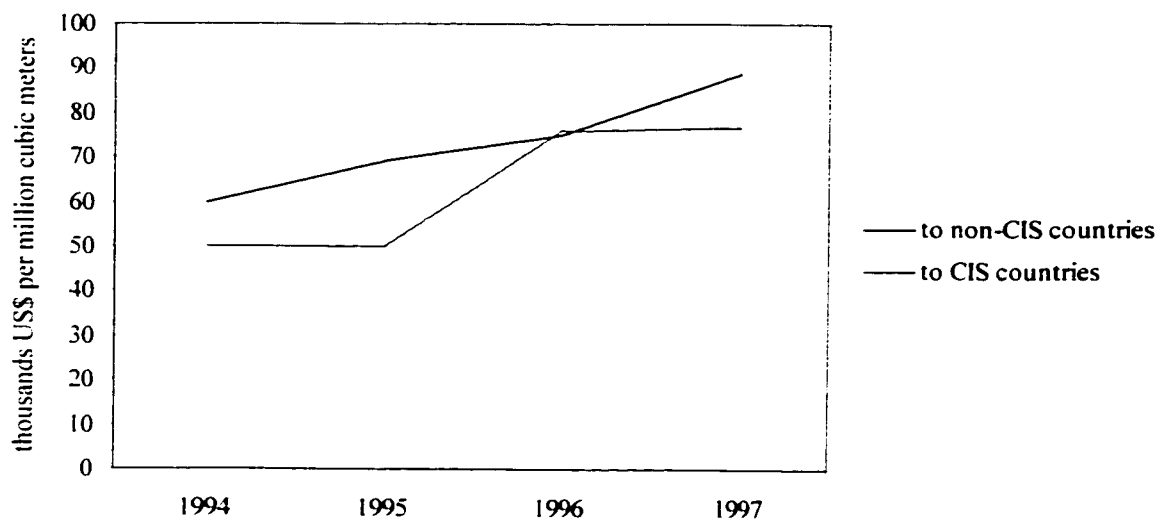


Figure 2.4 Average Price of Russian Exports, Natural Gas, 1994-1997

Source: State Ministry of Statistics of the Russian Federation, Special Report prepared for this study, October 1999.

#### IV. Energy Trade and the Survival of Subsidies

Russia employed a selective “carrot” (discounted energy prices and tolerance of nonpayments) and “stick” (energy cuts and embargoes) policy toward energy trade with

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<sup>29</sup> The convergence of prices in 1998 was driven by the fall in world market energy prices

the European NIS. Severe Russian fuel embargoes were implemented against the Baltic republics early in their struggle for independence. Subsequent shipment reductions to the European NIS were generally deployed purportedly as a penalty for nonpayments. However, the timing, duration and severity of Russian energy cuts depended less on the magnitude of the arrears and more on the policy noncompliance of the NIS in question.

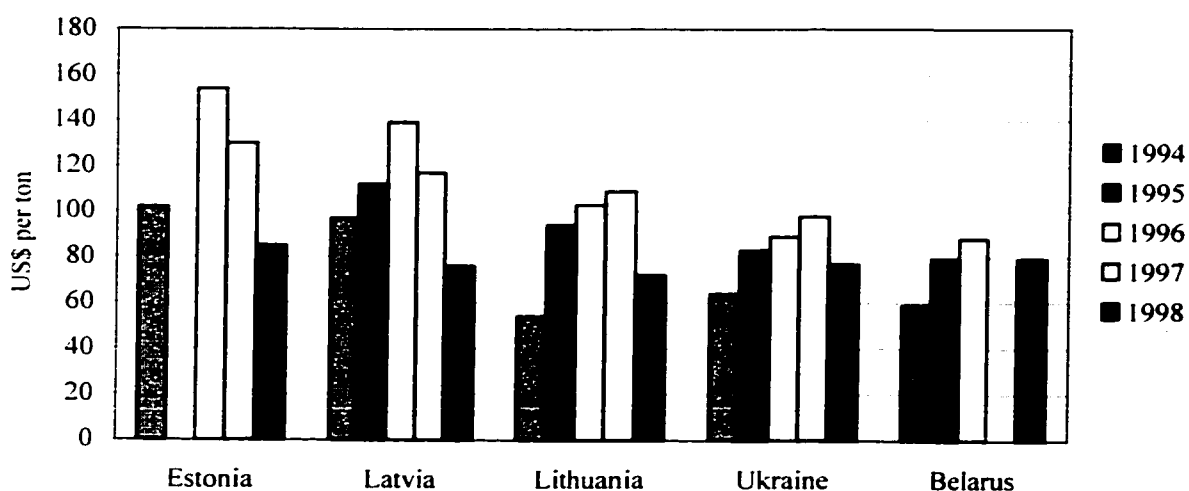


Figure 2.5 Russian Export Prices to Newly Independent States, Crude Oil, 1994-1998

Source: State Ministry of Statistics of the Russian Federation. Special Report prepared for this study, October 1999.<sup>30</sup>

precipitated by the Asian Crisis (for further discussion, see the Conclusion of this chapter).

<sup>30</sup> Data were not available in this series for selected years. Moldova did not import crude oil.

Russian “embargoes” on the Russophile Belarus amounted to empty threats or short-lived reductions in deliveries over issues of late payments. Energy cuts to the hybrids, Moldova, Ukraine and Lithuania, were often somewhat more substantial, and prices to these states higher. These cuts were also sometimes related to payments problems, but energy supply was also used in relation to issues of foreign policy, relations with the West and Western investors, and to the treatment of Russophone minority residents. While Lithuania suffered greatly due to the withholding of energy shipments early in its struggle for independence, it subsequently reached accommodation with Russia and suffered little from Russian embargoes after this. Lithuania also managed to maintain energy prices on some Russian imports comparable to those received by Ukraine and Moldova, and well below world market prices. The globalizers, Estonia and Latvia, also experienced severe energy shortages in the early days of independence, and they continued to suffer blockades in retaliation for policies of which Moscow disapproved. These states also paid much higher prices for the Russian energy imports. Despite Moscow’s grumblings about NIS nonpayments, it did permit arrears to grow, particularly those by Russophile and hybrid NIS (discussed below).<sup>31</sup>

Russia used the carrot of low energy prices and tolerance of nonpayments in response to NIS policy. Belarus was able to negotiate the most favorable prices, barter agreements, and tolerance of arrears of any of the European NIS. Ukraine, Moldova and Lithuania reached agreements to purchase Russian oil and natural gas, usually at well

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<sup>31</sup> The NIS chose different strategies in response to Russian energy trade policy, as reflected in the timing and degree of energy trade reorientation. The volume of imports from Russia and other trade partners is discussed in Chapter Three.

below world market prices. Unlike Lithuania, Latvia and Estonia chose to cope with the initial Russian energy embargo by beginning to reorient energy trade Westward rather than make policy concessions to Russia. When they purchased oil and gas from Russia, they usually did so for cash and at world market prices. The relative prices of Russian fuel exports reflect this. In 1995, the price of crude oil exports to non-CIS countries was 35% higher than to CIS countries. Natural gas prices for the same period were more than 50% higher. These lower prices, barter agreements and permissiveness of nonpayments amounted to large subsidizations of the NIS which chose to pursue them.

The Russophile, Belarus, remarkably consistently obtained the lowest prices for both crude oil and natural gas of the NIS. The hybrids, Lithuania and Ukraine, negotiated crude oil prices lower than world market prices and lower than those received by Estonia and Latvia. There was more variation in gas prices paid by the hybrids. Moldova was required to pay world market prices for gas until after 1994, when Russian and Moldova began to reach an accommodation on the Trans-Dniester conflict and after Moldova agreed to join the CIS. Ukraine benefited from below-world-market prices for gas until 1996, when Russian-Ukrainian relations began to sour. Lithuania paid world market prices for gas. The globalizers, Latvia and Estonia, paid much higher prices for both crude oil and natural gas imported from Russia than did any of the other NIS.

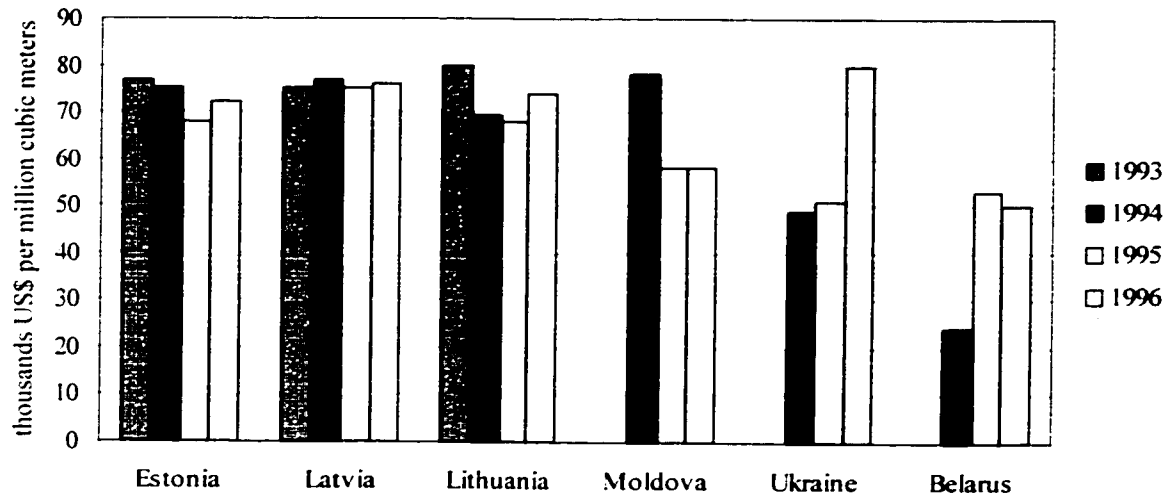


Figure 2.6 Russian Export Prices to Newly Independent States. Natural Gas, 1993-1996

Source: State Ministry of Statistics of the Russian Federation. Special Report prepared for this study, October 1999. <sup>32</sup>

Debts by Newly Independent States to Russia for energy deliveries grew enormously in the post-Soviet period, totaling \$3.9 billion by the end of 1996. Despite threats and brief shipment reductions by Russia, Moscow was remarkably tolerant of mounting debts by Russophile and hybrid NIS. Russia used forgiveness of this debt as a tool to secure control of domestic energy infrastructure within the NIS and to persuade NIS to enter into the CIS or other economic or political agreements with Moscow. Ukraine was the largest debtor, owing 3.69 trillion rubles to Moscow. Belarus owed over one trillion rubles, and Moldova over 2 trillion. All the Baltic states together owed only

0.123 trillion rubles.<sup>33</sup> The bulk of these debts were related to natural gas. Despite these debts, Russia continued shipments. Robert Ebel explains why:

Russian sales of natural gas to Ukraine, Belarus and Moldova serve as a form of foreign aid. Continued fuel supplies are vital to the political and economic stability of these importers, but these countries are not in a position to make little more than token cash payments for their imports.<sup>34</sup>

Belarus was the most successful in securing and maintaining Russian energy subsidies. Belarus was an enthusiastic founding member of the CIS and a signatory to all important treaties. Domestic critics alleged that conservatives in the Belarusian parliament had signed the CIS Collective Security agreement solely because of Belarus' dependence on cheap Russian oil.<sup>35</sup> Belarus did experience some fuel cuts from Russia because of nonpayments problems, but such reductions were relatively mild and short-lived. In August 1993, Russia cut gas deliveries to Belarus in order to elicit payment.<sup>36</sup> Gas supplies were increased the very next day<sup>37</sup>, after Belarus agreed to make good on a small percentage of arrears. Within a month, shipments were fully restored to previous levels.<sup>38</sup> Payments were to be made partly in cash and partly in barter for low-quality Belarusian products. More importantly, Belarus signed an agreement with Russia uniting the monetary systems of the two countries, promising to stay in the ruble zone, and placing the Belarusian state gas transportation company under the control of Russian gas

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<sup>32</sup> Data were unavailable in this series for selected years.

<sup>33</sup> Robert Ebel, *Energy Choices in the Near Abroad: The Haves and Have-Nots Face the Future* (Washington, D.C.: Center for Strategic and International Studies, 1997).

<sup>34</sup> Ibid., p. 27.

<sup>35</sup> Radio Free Europe/Radio Liberty, *Newsline* (May 26, 1993) "Russia to Cut Oil to Belarus."

<sup>36</sup> Radio Free Europe/Radio Liberty, *Newsline* (August 16, 1993) "Russia Cuts Gas to Belarus."

<sup>37</sup> Radio Free Europe/Radio Liberty, *Newsline* (August 17, 1993) "Russia Supplies Belarus with More Gas."

giant, Gazprom. In exchange for these concessions, Belarus received guaranteed levels of gas deliveries at highly discounted prices.<sup>39</sup> The next month Belarus signed an agreement regarding the proposed Yamal pipeline, which would transport Russian gas from Russia to Western Europe under Belarus, hoping to further guarantee access to cheap Russian energy.<sup>40</sup>

Similar nonpayment questions continued through 1998. Belarus failed to meet its payments obligations, despite low prices and highly favorable barter agreements.<sup>41</sup> Supply reductions were sometimes threatened but rarely implemented. When they did take place, they were usually small reductions lasting only a short time.<sup>42</sup> Belarusian arrears continued to mount, despite a "zero-option" agreement writing off all of Belarus' gas debt to Russia, signed in February 1996,<sup>43</sup> and various barter agreements for both oil and gas. Minsk argued for further debt forgiveness on the basis of the Belarusian-Russian economic union and the fact that Minsk allowed Russian troops to remain in Belarus free of charge.<sup>44</sup> By 1998, Belarus had secured agreements to pay for a full 75% of its gas in

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<sup>38</sup> Radio Free Europe/Radio Liberty, *Newsline* (September 7, 1993) "Russian Gas Supplies to Belarus Restored" and (August 25, 1993) "Russia Restores Gas to Belarus."

<sup>39</sup> Radio Free Europe/Radio Liberty, *Newsline* (September 13, 1993) "Belarus, Russia Sign Economic Agreement."

<sup>40</sup> Radio Free Europe/Radio Liberty, *Newsline* (October 13, 1993) "Belarus Hedging Cost of Oil on Pipeline."

<sup>41</sup> Radio Free Europe/Radio Liberty, *Newsline* (March 15, 1993) "Belarus Receives Reduced Gas Supplies"; (August 22, 1993) "Belarusian Gas Debt"; and (October 26, 1994) "Russia Cuts Oil to Belarus."

<sup>42</sup> Radio Free Europe/Radio Liberty, *Newsline* (January 6, 1997) "Gazprom Threatens Belarus with Gas Cuts"; (January 8, 1997) "Gazprom Won't Cut Gas to Belarus"; (July 21, 1997) "Russian Gas Supplies to Belarus to Continue at Current Levels"; (July 22, 1997) "Controversy Over Russian Gas Supplies to Belarus."

<sup>43</sup> Radio Free Europe/Radio Liberty, *Newsline* (January 6, 1997) "Gazprom Threatens Belarus with Gas Cuts."

<sup>44</sup> Radio Free Europe/Radio Liberty, *Newsline* (July 24, 1996) "Russian Deputy Prime Minister in Belarus."

barter.<sup>45</sup> Shipment continued despite Belarus' failure to meet even these low obligations. The Russian government extended loans to Belarus to assist in payments,<sup>46</sup> reduced the cash payment requirement from 25% to 20%,<sup>47</sup> and agreed to allow Belarus to pay very low Russian domestic prices for gas.<sup>48</sup>

Russia and Moldova reached agreements regarding energy shipments after Moldova agreed to join the CIS economic union and to ratify CIS membership,<sup>49</sup> sparing Moldova from the 1994 cuts in gas deliveries Russia meted out against other NIS in attempt to force payments.<sup>50</sup> Russia increased gas prices to Moldova, driving up arrears.<sup>51</sup> However, in 1995, Russia agreed to forgive massive portions of this debt,<sup>52</sup> to accept partial payment in agricultural barter,<sup>53</sup> and to guarantee a stable supply of Russian gas, in exchange for partial ownership and control of the Moldovan Gas company. While Russia repeatedly threatened to stop supplying Moldova with fuel, shutoffs were avoided by political and economic compromises with Moscow. Such deals were not without their detractors, however, and Moldovan leadership often fell victim to domestic criticism.

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<sup>45</sup> Radio Free Europe/Radio Liberty, *Newsline* (April 22, 1998) "Belarus, Gazprom Agree on Gas Debt Repayment."

<sup>46</sup> Radio Free Europe/Radio Liberty, *Newsline* (September 1, 1998) "Belarus May Receive Russian Loan, Pay for Gas by Barter."

<sup>47</sup> Radio Free Europe/Radio Liberty, *Newsline* (January 15, 1999) "Belarus to Pay Cash for 20 Percent of Russian Gas Supplies."

<sup>48</sup> Radio Free Europe/Radio Liberty, *Newsline* (March 18, 1999) "Gazprom Resumes Full Gas Deliveries to Belarus."

<sup>49</sup> Radio Free Europe/Radio Liberty, *Newsline* (November 5, 1993) "Moldova Damaged by Russian Economic Pressure."

<sup>50</sup> Radio Free Europe/Radio Liberty, *Newsline* (March 4, 1994) "Gas Supplies Reduced."

<sup>51</sup> Radio Free Europe/Radio Liberty, *Newsline* (May 20, 1994) "...And Pre-Payment for Gas."

<sup>52</sup> Radio Free Europe/Radio Liberty, *Newsline* (May 16, 1995) "Moldovan-Russian Gas Agreement."

<sup>53</sup> Radio Free Europe/Radio Liberty, *Newsline* (August 21, 1995) "Moldova Attempts to Cope with Gas Debt."

The opposition objected to President Lucinschi's strategy of dealing with Russia as "selling out the country's independence for gas and oil."<sup>54</sup>

Russian supply cuts to Ukraine were short-lived and related to nonpayments problems. In 1993, Russia began to raise prices substantially in oil and gas exports to Ukraine.<sup>55</sup> Debts began to mount, and Russia briefly reduced supplies of oil<sup>56</sup> and natural gas.<sup>57</sup> In response, Ukraine increased transportation fees for the quite substantial volume of gas<sup>58</sup> and oil exported from Russia to Western Europe through Ukraine, and was also suspected of siphoning off gas designated for Western Europe for its own purposes.<sup>59</sup> The dispute was soon resolved when Ukraine agreed to sign over to Russia shares of Ukraine's national gas distributor, gas transport and storage facilities, and to build housing for Russian workers in exchange for its debt.<sup>60</sup> Disagreements over prices, transit fees, and supplies continued for years, but while Russia repeatedly made threats to cut off gas to Ukraine, it failed to carry them out. As late as 1997, Ukraine remained Russia's largest natural gas customer.<sup>61</sup>

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<sup>54</sup> Radio Free Europe/Radio Liberty, *Newsline* (March 9, 1998) "Lucinschi on Relations with Russia, NATO."

<sup>55</sup> Radio Free Europe/Radio Liberty, *Newsline* (January 12, 1993) "Russian-Ukrainian Oil Dispute."

<sup>56</sup> Radio Free Europe/Radio Liberty, *Newsline* (April 6, 1993) "Russian-Ukrainian Gas Dispute Still Unresolved."

<sup>57</sup> Radio Free Europe/Radio Liberty, *Newsline* (August 27, 1993) "Russia Cuts Gas Supply to Ukraine."

<sup>58</sup> 90% of the natural gas exported from Russia to the hard currency markets of Western Europe traversed Ukraine.

<sup>59</sup> Radio Free Europe/Radio Liberty, *Newsline* (August 16, 1994) "Ukraine to Hold Talks with Gazprom."

<sup>60</sup> Radio Free Europe/Radio Liberty, *Newsline* (August 16, 1994) "Ukraine to Hold Talks with Gazprom."

<sup>61</sup> Radio Free Europe/Radio Liberty, *Newsline* (September 12, 1997) "Ukraine to Remain Biggest Consumer of Russian Natural Gas."

Lithuania suffered a prolonged fuel embargo in response to its bid for independence in 1990. Russia cut off all oil shipments and 80% of natural gas shipments in April 1990.<sup>62</sup> Lithuanian resources were quickly depleted, and Lithuania agreed to suspend its declaration of independence. Russia resumed fuel shipments, though energy supply remained a central tool of Russian policy throughout Lithuania's struggle for independence, 1990 through early 1992. After independence, however, cuts in oil and gas supplies were brief, and were related primarily to economic (payments) rather than political goals. In the spring of 1992, quota and barter agreements were concluded between the two to normalize fuel sales to Lithuania.<sup>63</sup> Gas and oil supplies were briefly reduced in the autumn of that year,<sup>64</sup> and again in the summer of 1993,<sup>65</sup> due to payments problems. These reductions were ended with promises by Lithuania of payments and the possibility of Russian partial ownership of Lithuanian oil and gas concerns.<sup>66</sup> A third oil supply interruption took place in August of 1994, although this time due to production problems in the Russian fuel industry.<sup>67</sup> Gas shipments were reduced in January 1996 because of payment problems,<sup>68</sup> and again in April 1999.<sup>69</sup>

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<sup>62</sup> "Soviets Cut Lithuanian Gas: Soviet Bases, Plants to be Hit First" *Associated Press* April 19, 1990. Online. LEXIS-NEXIS Academic Universe.

<sup>63</sup> Radio Free Europe/Radio Liberty, *Newsline* (March 9, 1992) "Lithuania-Russia Trade Agreements Signed" and (March 6, 1992) "Agreement with Russia for Oil and Gas."

<sup>64</sup> Radio Free Europe/Radio Liberty, *Newsline* (August 31, 1992) "Russia Decreases Gas Supplies to Lithuania" and (October 13, 1992) "Russia to Resume Oil Supplies to Lithuania."

<sup>65</sup> Radio Free Europe/Radio Liberty, *Newsline* (July 12, 1993) "Russia Restores Gas Supply to Lithuania."

<sup>66</sup> Radio Free Europe/Radio Liberty, *Newsline* (July 29, 1993) "Talks Continue on Lithuanian-Russian Gas joint Venture."

<sup>67</sup> Radio Free Europe/Radio Liberty, *Newsline* (September 2, 1994) "Russian Oil Shipments to Lithuania Resume."

<sup>68</sup> Radio Free Europe/Radio Liberty, *Newsline* (March 8, 1996) "Lithuania's Energy Problems."

<sup>69</sup> Radio Free Europe/Radio Liberty, *Newsline* (April 27, 1999) "Lithuania Still Receiving Gas from Russia."

Like Lithuania, Estonia and Latvia also suffered Russian fuel cuts and embargoes during their struggle for independence in 1990 - early 1992. And, like Lithuania, both Estonia and Latvia experienced severe energy crises, particularly in the winter of 1991-1992.<sup>70</sup> Unlike Lithuania, however, Estonia and Latvia immediately began energy trade reorientation during these fuel shortages. Russian energy prices soon rose, and in early 1992, Estonia concluded agreements to purchase Russian oil products at world market prices<sup>71</sup> (in addition to its growing imports from the West). In September 1992, Estonia and Russia negotiated an agreement to normalize trade relations between the two, and to guarantee a certain level of energy supplies to Estonia.<sup>72</sup> Latvia concluded a similar agreement in October of that year.<sup>73</sup> Unlike with the other NIS, Russian threats to Estonia and Latvia to cut energy supplies were carried out with enthusiasm. In 1993, Estonia was the target of a Russian fuel embargo, not because of Estonian debt, but because of Estonian citizenship policies regarding Russophone minorities. On June 25, Russia cut off natural gas supplies to Estonia.<sup>74</sup> (An oil embargo would have been meaningless, as Estonia was already importing a substantial portion of its oil from the West.) But by this time Estonia was paying hard currency for its gas imports, and possessed the capacity to import liquefied natural gas from the West. Ironically, the

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<sup>70</sup> Radio Free Europe/Radio Liberty, *Newsline* (December 27, 1991) "Fuel Shortage in Estonia"; (January 14, 1992) "Estonian Water Runs Cold"; (January 30, 1992) "Gas Price Skyrockets in Latvia"; (January 8, 1992) "Riga Buses Running Out of Fuel"; (January 9, 1992) "Fuel Shortages Continue in Latvia"; (January 29, 1992) "Energy Crisis in Latvia Worsens."

<sup>71</sup> Radio Free Europe/Radio Liberty, *Newsline* (January 24, 1992) "Fuel Deliveries for Estonia."

<sup>72</sup> Radio Free Europe/Radio Liberty, *Newsline* (September 8, 1992) "Russia, Estonia Sign Trade Agreement."

<sup>73</sup> Radio Free Europe/Radio Liberty, *Newsline* (October 29, 1992) "Latvian-Russian Economic Accords."

embargo hurt most those whom it was intended to help, as gas was disproportionately consumed by industry, and ethnic Russians comprised 75% of the industrial workforce.<sup>75</sup> Russian threatened Latvia with similar sanctions because of alleged discrimination against Russophile residents.<sup>76</sup>

## **V. Conclusion: The Future, and Fragility, of Russian Fuel Subsidies**

Russia left the door open to all the European NIS to maintain subsidies in exchange for political concessions, and did not hesitate to withhold energy shipments when NIS policies displeased it. The Commonwealth of Independent States was open to all the NIS, including the Baltic states. Those who joined on average enjoyed lower energy prices and a greater reliability of supply from Russia. Russia was also willing to extend energy subsidies to non-CIS NIS in exchange to political cooperation, as demonstrated by the case of Lithuania. However, the value of these energy subsidies in the long run must be questioned.

The "Asian Crisis" which began in late 1997 soon became a global phenomenon, sending shock waves through emerging markets and developed economies alike. Russia was particularly hard hit. The ramifications of the Asian downturn for Russia were two fold. First, the collapse of the banking and investment sectors in the Asian tigers, the

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<sup>74</sup> "Estonians React Calmly to Russia's Cutoff of Gas" *Associated Press* June 25, 1993. Online. LEXIS-NEXIS Academic Universe.

<sup>75</sup> "Angry Russia Cuts Off Gas to Estonia; Embargo: The Stoppage Comes a Day After President Yeltsin Threatened Reprisals for What He Called the Baltic State's 'Apartheid' Policy" *Los Angeles Times* June 26, 1993. Online. LEXIS-NEXIS Academic Universe.

<sup>76</sup> Radio Free Europe/Radio Liberty, *Newsline* (April 9, 1998) "Moscow Denies Plans for 'Total Embargo' of Latvia"; (July 3, 1998) "...While Moscow Denies Imposing Sanctions on Latvia"; (July 10, 1998) "Federation Council Calls for Action Against Latvia."

supposed models of quick industrialization and the envy of the developing world, substantially undermined the confidence of international investors in emerging markets. If such a disaster could take place in the seemingly robust economies of East Asia, who was to say that collapse was not imminent in obviously more troubled economies such as Russia's? Both portfolio investment and direct foreign investment dramatically decreased in Russia, robbing it of much-needed capital.

Secondly, the contraction of the economies of the Asian Tigers, increasingly important consumers of oil, combined with an increase in global oil production, served to undermine the price of oil and other fuels on the international market. Russia relied on oil and gas exports as its principal source of hard currency. In the late post-Soviet period, these revenues had become increasingly important. Russia saw capital hemorrhaging from its borders at the same time that it had to produce more oil for less income. Moscow now had difficulty subsidizing its energy exports to allies in the near abroad. By April 1998, discounts on Russian crude oil exports to CIS members had come to an end. In fact, because of increases in Russian prices to the CIS and dramatic decreases in world market prices, prices for hard-currency buyers were now slightly lower.

Table 2.1 Average Export Prices of Crude Oil from Russia, 1997-1998

	Importer	
	CIS countries	Non-CIS countries
January-April 1997	\$91.40 per m.t.	\$127.75 per m.t.
January-April 1998	\$94.09 per m.t.	\$84.46 per m.t.
April 1998	\$85.30 per m.t.	\$81.24 per m.t.

Source: Energy and Politics *Pipeline News*, No. 23 (1998). Russian State Customs Committee, Interfax, June 30 1998.

Russia's implicit acceptance of nonpayments for energy supplies to the near abroad also faltered as Russia rushed to collect some much-needed cash. In May 1998, Gazprom announced that it would cut deliveries of natural gas to Belarus by 40% beginning on June 15th. because of Belarus' failure to pay its gas debt to Russia as agreed upon in April. Russia did in fact reduce deliveries in June after Minsk failed to produce payment.<sup>77</sup> At the same time, Gazprom cut deliveries to Moldova in half, again for nonpayment.<sup>78</sup> Only Ukraine was making satisfactory enough progress toward repayment to deter Gazprom from reducing shipments. Ukraine has been making its payments, albeit for the most part in kind rather than in cash.<sup>79</sup>

The timing of Gazprom's crackdown on debtors was not coincidental. Because of the desperate financial straits in which the Russian government found itself in early 1998, the Russian State Tax Service began to put pressure on Gazprom to pay its tax debt, in cash. The state demanded that Gazprom collect at least 60% of its gas sales in cash, in order for Gazprom to have the money to pay its taxes. This placed Gazprom in a tenuous position, as CIS members paid cash for only 1% of Gazprom gas in 1997, and usually paid late. The situation had not improved much in the first half of 1998, with Moldova paying for only 3% of gas imports in cash, and Belarus for 4.6%. Gazprom was forced to reduce shipments.<sup>80</sup>

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<sup>77</sup> Energy and Politics *Pipeline News*, No. 23 (1998), Interfax, June 15 1998; Itar-Tass, June 18 1998; Izvestiya, June 17 1998.

<sup>78</sup> Energy and Politics *Pipeline News*, No. 23 (1998), RIA-Novosti, June 15 1998.

<sup>79</sup> Energy and Politics *Pipeline News*, No. 23 (1998), Interfax, June 24 1998.

<sup>80</sup> Energy and Politics *Pipeline News*, No. 23 (1998), Interfax Daily Business Report, June 24 1998.

As international energy markets recovered after the Asian Crisis, demand for energy began to increase again, and OPEC producers agreed to reduce supply. These factors combined to send oil prices to record highs again by 2000. As the financial pressure on Russia eased, so did the pressure it applied to its CIS customers. Selective subsidies and tolerance of growing arrears soon returned. This episode is important, however, in demonstrating the precarious nature of a long-term economic strategy based on subsidies from Russia. Russia has shown a willingness to continue energy subsidies to the NIS in exchange for political concessions such as joining the CIS. It has demonstrated a willingness to cut subsidies and suspend shipments when a NIS does not comply with Russian political demands, both in the spheres of foreign and domestic affairs. However, Russia can no longer continue to masquerade as a major economic power. It is itself highly vulnerable to the slings and arrows of international commodity markets and the whims of the "electronic herd."<sup>81</sup> Russia continues to pursue power and influence in the "near abroad." However, in times of domestic crisis, it has become clear that these foreign policy goals are secondary.

Therefore, while reliance on Russian subsidies may have proven less difficult in the short-run for economies and elites in some NIS, in the long run the strategy will likely prove much more difficult and perhaps, in the end, unsustainable. Dependence on Russian largesse may prove disastrous in the not unlikely event that Russia enters another period of crisis. Such a crisis could be precipitated by any number of factors, such as the

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<sup>81</sup> Thomas Friedman uses the "electronic herd" to describe the fickle international community of portfolio investors and currency speculators who now, thanks to advancements in communication and computer technology, have the ability to flood or deprive instantly foreign markets of capital. *The Lexus and the Olive Tree: Understanding Globalization* (New York, N.Y.: Farrar, Straus, Giroux, 1999).

spread of secessionist movements within Russia, requiring large amounts of state resources for their suppression; a massive unemployment crisis precipitated by efforts at fiscal balance, economic rationalization, or the ending of domestic nonpayments problems; another plunge in energy prices on the infamously volatile international energy markets, etc. Those states which have severed their dependence on Russia's economy will indeed be grateful for this should that economy again begin to sink.

## **CHAPTER III**

### **BETWEEN TWO WORLDS: POST-SOVIET EUROPEAN STATES**

#### **I. Coalitions and Energy Strategies**

It is conventional wisdom that industrialization is a step toward economic development, and that an industrial base should facilitate further economic growth. However, the development of heavy industry in the European NIS proved a drag on change after the Soviet collapse. The bulk of industry in the European NIS was the product of forced industrialization, and in many cases, forced Russification, by the Soviet regime. In the Soviet era, industry, heavy industry in particular, accounted for a disproportionate share of energy consumption in the European republics. In turn, natural gas and oil (both of which were imported from Russia) accounted for a disproportionate share of industrial energy consumption. Heavy industry in the European republics depended fundamentally on Russian energy imports. Energy trade reorientation, which would entail increasing prices and decreasing supplies of gas and oil, would therefore be borne disproportionately by industry. To the extent that the state was insulated politically from this energy-intensive sector, it was more likely to be able to sustain pro-globalist coalitions and policies that promoted energy trade diversification. Energy trade diversification went hand-in-hand with economic marketization and greater de facto political independence from Russia.

This chapter outlines a comparative analysis of the change in energy trade vulnerability and orientation of the European NIS. I examine consumption -- and

specifically industrial consumption -- of oil and natural gas, the availability of indigenous energy resources, and analyze of energy trade patterns of the European NIS. None of these states possessed sufficient resources to attain energy autarky. I argue that industry not only consumed a disproportionate share of energy, but also a disproportionate share of those energy inputs (natural gas and oil) imported from Russia. Thus, industry was particularly dependent on sustaining energy subsidies from Russia, making energy trade policy especially salient to this sector. Ruling coalitions more politically insulated from industry were thus better able to reduce dependence on Russian energy imports.

I begin by outlining the typology of political coalitions and the composition of the ruling coalitions in the cases. The globalizers were dominated by right-wing reformist coalitions. The hybrids experienced oscillation between coalition types and/or divided, ineffectual rule. The Russophile was dominated by left-wing conservative industry-backed coalitions. In the next section, I summarize the level of energy trade and vulnerability in the six cases. The globalizers experienced the greatest reduction in energy vulnerability to Russia. The hybrids experienced little to moderate change. The Russophile experienced no change, remaining entirely dependent on Russia for energy. I then turn to a more detailed discussion of energy use, economic performance, overall energy consumption and industrial energy consumption for each case.

### *Coalitions and ethnic minorities*

The presence of a substantial, sectorally (and in some cases geographically) concentrated, relatively less organized and mobilized ethnic minority can facilitate

energy trade reorientation. The state's ability to foist the costs of energy trade reorientation upon this minority, and then to politically disenfranchise this population, can give the state the ability to initiate and maintain these costly "globalizer" policies. This condition is met in the globalizers. It is absent in the Russophile. This condition may or may not be met by the hybrids: it is absent in Lithuania; Moldova possesses a substantial, concentrated minority, though it is highly organized and mobilized; Ukraine comes closest to meeting the condition.

Political coalitions in the European NIS tend to form according to a fairly consistent logic. The first sort of coalition draws in members in favor of economic marketization, liberalization and privatization. These coalitions also support economic opening and internationalization to the international market. They also favor strong ties with Western European and American, that is, "Western," international organizations and markets and a political and economic distancing from Russia. Because of the specific legacies of Stalinist industrialization discussed in previous chapters, these coalitions also often draw upon nationalist ideas of ethnic or linguistic exclusion. They draw social support from the more competitive, less energy-intensive sectors of the economy, particularly those with export potential; those which benefit from privatization, such as many small businesses and new entrepreneurs; on emerging sectors, such as services and tourism; and upon urban intellectuals and nationalists. These right-wing reformist coalitions are "globalist" coalitions.

The second type of coalition is in favor of preservation of the socialist economy and social security net and of the state-led economy. This coalition opposes opening to

the international market and the globalization of the economy. They favor continued strong political and economic ties with Russia, particularly the continuation of energy subsidies. They advocate membership in the CIS perhaps to the exclusion of membership in Western organizations. Their social foundation is based on uncompetitive, energy-intensive sectors of the economy, particularly heavy industries like chemicals, metallurgy, machine-building, and defense; on bureaucrats and public employees whose power and livelihoods depend on the economy remaining state-owned; and dedicated Communist and Socialist constituencies. These left-wing conservative coalitions are the Russophile coalitions.

Table 3.1 Ruling Coalitions and Energy Trade Strategies in the European NIS

Country	Strategy	Coalitions
Estonia	Globalizer	<p>Domination by globalist coalitions.</p> <p>1990-: globalist coalitions: pro-market reform, pro-internationalist, anti-Russian coalitions.</p> <p>1990 parliamentary elections: right-wing, pro-reform, pro-independence Popular Front-led coalition.</p> <p>1992 parliamentary elections: right-wing, pro-reform, anti-Russian Pro Patria-led coalition: right-wing Meri elected president.</p> <p>1995 parliamentary elections: center-right, pro-reform, anti-Russian coalition.</p> <p>1996 presidential elections: right-wing Meri.</p> <p>1999 parliamentary elections: right-wing coalition.</p>
Latvia	Globalizer	<p>Series of globalist and moderate globalist coalitions.</p> <p>1990-95: globalist coalitions: pro-market reform, pro-internationalist, anti-Russian coalitions. 1990 parliamentary elections: right-wing, pro-reform, pro-independence, anti-Russian Latvian Popular Front: Gorbunovs president. 1993 parliamentary elections: right-wing, pro-market reform, anti-Russian Latvian Way Union; anti-Russian Ulmanis president.</p> <p>1995-97: moderated globalist coalition: parliamentary elections: center-right, fragmented legislature. Centrist Master Democratic Party initially dominates ruling coalition. 1996 presidential elections: Ulmanis reelected.</p> <p>1997-: return to strong globalist coalitions: right-wing reorganization of parliament in favor of market reform.</p>

Table 3.1 Ruling Coalitions and Energy Trade Strategies (cont.)

Lithuania	Hybrid	Oscillation and division. Alternation between left and right coalitions, absence of dominant coalition. 1990-92: globalist coalition: 1990 parliamentary elections: right-wing, pro-market reform, pro-independence Lithuanian Reform Movement; Landsbergis elected president. 1992-96: left-wing compromise coalition. 1992 parliamentary elections: left-wing, pro-accommodation with Russia Lithuanian Democratic Labor Party; Brazauskas elected president. 1996-: moderate globalist coalition: 1996 parliamentary elections: right-wing, pro-market reform Homeland Union. 1997 presidential elections: right-wing, pro-market reform, pro-internationalist, Adamkus
Moldova	Hybrid	Oscillation and division. Alternation between left and right coalitions, absence of dominant coalition. 1990-1994: division between globalist and Russophile coalitions. 1990 parliamentary elections: fragmented legislature: pro-independence, anti-Russian, pro-nationalist Popular Front of Moldova and pro-Socialist, pro-Russian Communists. (Snegur president from 1989 election.). 1991: split parliament leads to ouster of PM, after which PFM and Snegur take position which are pro-independence, pro-accommodation with communists. 1991 presidential elections: pro-independence, pro-accommodation with communists Snegur. 1994-: compromise coalitions: 1994 parliamentary elections: left-wing, pro-independence, anti-market reform, pro-accommodation with Russia Democratic Party of Moldova. 1996 presidential elections: left-wing, pro-Russian, pro-CIS Lucinschi. 1998 parliamentary elections: left-wing, pro-Russia Communist Party plurality, with DPM minority
Ukraine	Hybrid	Oscillation and division. Alternation between left and right coalitions, absence of dominant coalition. 1991-1994: division. 1991 presidential elections: reformist Kravchuk, must share power with powerful conservative parliament. 1994-: compromise coalitions: 1994 presidential elections: left-wing, pro-communist, pro-industrialist, pro-Russian Kuchma. 1994 parliamentary elections: left-wing pro-communist, pro-Russian, anti-market. 1998 parliamentary elections: left-wing reelected, with stronger Communist faction.
Belarus	Russophile	Consistent pro-Russian, pro-socialist coalitions. 1990-1994: Russophile coalition with some division. 1990 parliamentary elections: leftist, pro-communist, pro-Russian coalition. 1991 presidential elections: center-right pro-market, pro-independence Shushkevich elected, but policies constrained by left-wing parliament. 1994-: Russophile consolidation. 1994 presidential elections: left-wing, pro-Russian, pro-communist, anti-Western Lukashenko. Subsequent presidential elections suspended. 1995 parliamentary elections: left-wing, pro-communist, pro-Russian coalition of Communists, Agrarians, and Conservatives

Domination by pro-market, pro-West, globalist coalitions is underwritten by the first condition: the exclusion of those suffering worst from reforms helps to maintain the power of the coalition. The globalizers were indeed dominated by such coalitions. The Russophile was dominated by the opposite type of coalitions: socialist, pro-Russia, pro-status quo coalitions. The hybrids experienced either oscillation between coalition types, states divided between opposing coalitions, or domination by “compromise” coalitions, leading to policy inconsistency and/or compromise and little change in energy dependence on Russia.

## **II. Energy Use and Trade**

Vulnerability to Russian energy supplies cannot be summed up simply in one figure. States may seek to reduce vulnerability through decreasing consumption, increasing efficiency, increasing the use of domestic resources, decreasing overall imports, decreasing imports from Russia while increasing imports from the West, or maintaining imports from Russia while restructuring incentives (such as ownership and payments to Russia) and control (notably to Western partners who will ensure supply should Russia suspend shipments). These strategies may be summarized by a small number of indicators.

The reduction of energy vulnerability to Russia – the “dependent variable” – is operationalized using three indicators: change in the overall dependence on energy imports; change in energy imports from Russia; and the level of strategic “balancing”

investment and ownership arrangements in the energy sector.<sup>1</sup> Change in the overall dependence on imported energy, as measured by net energy imports as a share of energy consumption (see Tables 3.8-3.12), indicates the level to which the state had increased energy efficiency and the development of domestic resources as alternatives to its reliance on external energy sources. The change in energy imports from Russia indicates, to the extent that the state is still dependent on imports, the degree to which it is dependent on Russia. The level of strategic “balancing” investment, that is, shared or whole ownership of domestic energy resources, distribution, processing or infrastructure by Western companies, indicates the reduction of vulnerability in energy sectors in which the state remained dependent on Russia for supply.

Globalizers, which seek to reduce their vulnerability to Russian energy supply interruptions, do so by reducing dependence on energy imports, diversifying the sources of those imports to the greatest extent possible, and by seeking private Western and other investors in the energy sectors the supply of which they are unable to reorient to new suppliers. A Russophile, by contrast, will seek to maintain the level and source of energy imports to the greatest extent possible. Little emphasis will be placed on reducing imports as long as subsidized prices can be maintained, and other suppliers and owners would not be sought. Hybrids, because of their political compositions, will pursue

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<sup>1</sup> Electricity imports from Russia are not a good measure of energy dependence on Russia for several reasons. First, many of the European NIS possessed independent electricity-generating capacity, including the potential to export in many cases. Secondly, electricity imports, even during the Soviet era, were just as often from another Soviet republic as they were from Russia. Some European NIS did not import electricity at all. To the extent that electricity generation within the republics was not based in indigenous resources but on imported fuel, they were based in oil and natural gas imports from Russia. Thus, most of the electrical energy dependence which may have existed can be measured in the oil and gas imports from Russia.

elements of both strategies, often in conflict with one another. Because of the political resources necessary (but unavailable) to reorient energy trade, they will achieve relatively less reduction of dependence on energy imports, less diversification of those imports. They may not seek, or they may seek less successfully, the same level of strategic investment as the globalizers.

Table 3.2 Change in Energy Vulnerability to Russia

	Reduction in energy import dependence	Share of imports from Russia (oil) <sup>2</sup>	Reduction of dependence on Russia (oil) <sup>2</sup>	Level of strategic balancing investment
<i>Globalizers</i>	High	Low	High	High
- Estonia	<sup>3</sup> 32%	42%	<sup>3</sup> 71%	high
- Latvia	35%	65%	58%	high
<i>Hybrids</i>	Moderate to none	Moderate to high	Moderate	Moderate to low
- Lithuania	25%	94%	30%	moderate
- Moldova	0%	<sup>4</sup> 88%	12%	low
- Ukraine	15%	<sup>4</sup> 65%	45%	moderate
<i>Russophile</i>	Negligible	High	Negligible	Negligible
- Belarus	2%	98%	2%	none

Sources: International Energy Agency, Interstate Statistical Committee of the Commonwealth of Independent States, Statistical Office of Estonia, Statistical Department of Lithuania, State Committee for Statistics of the Republic of Latvia, State Commission of Statistics and Analysis of the Republic of Belarus.

<sup>2</sup> Because of the prohibitively high costs of alternative infrastructures, Russia remains the sole supplier of natural gas to all European NIS. Those states which have sought security of supply in this sphere have done so through strategic balancing investments. Therefore, only the diversification of oil imports (the other principal energy import) are analyzed here.

<sup>3</sup> Estonia began its oil reorientation earlier than did the other cases, prior to the reassertion of independence. Therefore, a comparison of 1997 levels with those of 1990 (rather than 1991, as in the other cases) is a more accurate measure of the decrease in dependence on imports. 1990 figures are used here. See Statistikaamet, *Statistical Yearbook of Estonia 1999*, p 271.

<sup>4</sup> These are approximations based on the best and most recent figures available, which may not be entirely compatible with other data sets.

As expected, globalizers exhibit the greatest reduction of dependence on imports of all cases. The Russophile experienced virtually no change. The hybrids ranged from moderate to no change, depending greatly, in our cases, upon the possibility of developing indigenous energy resources (of which Moldova had none). The percentage of energy imports from Russia is lowest in the globalizers, higher in the hybrids, and virtually unchanged in the Russophile. The level of strategic balancing investment was also highest in the globalizers, lower in the hybrids, and nonexistent in the Russophile.

The remainder of this section outlines the consumption of energy, and oil and natural gas in particular, by industry in the European NIS and the restructuring of energy consumption and trade since independence. It then briefly examines the indigenous energy resources available to these states. Lastly, it explores patterns in European NIS energy trade, specifically, changes in production and trade volume.<sup>5</sup>

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<sup>5</sup> Studying the process of political and economic transitions offers many exciting advantages and opportunities to the researcher. Data availability and quality are not among them, however. Economic data for the transition period, particularly the years of 1989, 1990, 1991 and 1992 is often nonexistent, and where it is available, is incompatible with data collected in subsequent years. Soviet-era data reporting and collection procedures differ infamously from established international standards, sometimes bearing more resemblance to political goals than to economic reality. In addition to this challenge, during 1989-1992, when institutions and accountability structures were in flux, data was often simply not collected.

Some of the most reliable data were available from the International Energy Agency, though it does not differentiate among NIS until 1992, and warns that 1991-1992 data are not comparable to those that follow. The Interstate Statistical Committee of the Commonwealth of Independent States is the best source for more detailed energy data on Ukraine, Moldova and Belarus, as well as for Russian exports, though the CIS data series are most often incomplete. The best and most consistent data sets are available from the statistical ministries of Latvia and Estonia, though of course these data sets begin only after the early transition period. Similar data are available from the Lithuanian statistical ministry, though the data compilation and collection procedures in Lithuania have been less consistent than in Latvia and Estonia. Nevertheless, sufficient data are available on energy consumption and trade of the European NIS to establish post-independence patterns.

*Industrial consumption of oil and natural gas*

The political preferences of dominant coalitions, not merely aggregate economic concerns, determine the energy trade strategy of the state. If energy trade strategy were determined purely by economic and not political forces, one would expect that those states which required the most energy per capita or per unit of output would have been the most reluctant to give up energy trade subsidies from Russia, as they would be the most injured by rising energy prices. However, the energy intensity at the time of independence, that is, the amount of energy necessary to produce a unit of output, was not a good predictor of subsequent energy trade policy toward Russia. In fact, Ukraine, Estonia and Belarus, the states with the highest energy use per capita and highest energy use per unit of GDP in 1992, adopted radically different strategies regarding their energy dependence on Russia. Moldova and Lithuania used much less energy per unit of GDP than their fellow hybrid Ukraine, with Lithuanian consumption at about half of Ukraine's. Latvia used least of all, and yet adopted a globalizer strategy like the relatively energy-intensive Estonia.

Table 3.3 Energy Use Per Capita (toe per capita)

	1992	1993	1994	1995	1996	1996 as % of 1992
Estonia	4.359	3.675	3.818	3.616	3.834	88%
Latvia	2.4	1.886	1.808	1.581	1.675	89%
Lithuania	2.997	2.432	2.117	2.365	2.414	81%
Moldova	1.626	1.345	1.101	1.015	1.063	65%
Ukraine	4.233	3.723	3.186	3.141	3.035	72%
Belarus	3.884	3.012	2.562	2.329	2.386	61%

Source: International Energy Agency, *Energy Statistics and Balances, 1991-1992, 1992-1993, 1993-1994, 1994-1995, 1995-1996*. 1991 and 1992 series are not entirely comparable with recent years due to differences in data reporting procedures.

Subsequent patterns in energy use per unit of GDP indicate trends in the energy efficiency of the European NIS. The globalizers experienced increases in their energy efficiency after 1992, due to restructuring in their domestic economies (closure of inefficient industries) and growth of their GDP. The hybrids all experienced declines in efficiency, driven by less restructuring and the slow recoveries of their poorly performing overall economies. Energy efficiency in Lithuania and Moldova fluctuated around 1992 levels since independence, while the latter managed to realize gains in 1997. Ukrainian energy efficiency simply declined since independence. Belarus, the Russophile, through concentrated government programs experienced an increase in energy efficiency as well. While there was some decline in gas consumption, oil consumption levels remained high.

Table 3.4 Gross Domestic Product of the European NIS, 1992-1997 (billion US\$90)

	1992	1993	1994	1995	1996	1997	1997 as % of 1992
Estonia	4.9	4.5	4.4	4.6	4.8	5.3	108%
Latvia	7.3	6.2	6.2	6.2	6.4	6.8	93%
Lithuania	9.8	8.2	7.4	7.7	8.1	8.5	87%
Moldova	6.7	6.6	4.5	4.4	3.9	4.0	60%
Ukraine	129.1	110.8	85.3	74.9	67.4	65.2	50%
Belarus	31.2	28.8	25.2	22.6	23.2	25.6	82%

Source: International Energy Agency. *Energy Balances of Non-OECD Countries, 1996-1997*, p. II.427, (1999).

The economies of the globalizers, Estonia and Latvia, experienced initial declines but soon began to recover. The Estonian economy began to grow in 1995, and by 1997 exceeded pre-independence production. Latvia's economy was slower to recover, plateauing in 1993-1995, but beginning to grow thereafter. The economy of the Russophile declined gradually after independence, but began to grow slowly again in

1996. The economies of the hybrids also experienced declines, though while Lithuania's staged a moderate comeback and Moldova's began growth finally in 1997, Ukraine's economy continued to shrink. By 1997, Ukraine's economy had sunk to only half of its 1992 level.

The energy-intensive industries of the European NIS at the dawn of independence were especially dependent on natural gas, and to a lesser extent in many cases, oil, both of which were imported from Russia. To the extent that the consumption of these imports were concentrated in heavy industry, the ramifications of rising prices and supply shortages were felt most acutely by those sectors. In the cases where the bulk of an energy input (such as natural gas) was consumed by industry, the difficulties associated with the move to world markets were largely isolated to industry. In cases where the government was more politically insulated from industry, changes in energy trade policy with Russia were politically easier to implement, whereas governments which relied heavily on industry for support found it imperative to attempt to maintain Russian energy subsidies.

Table 3.5 Energy Use per GDP (toe per thousand 90 US\$)

	1992	1993	1994	1995	1996	1997	1997 as % of 1992
Estonia	1.34	1.17	1.25	1.12	1.18	1.04	78%
Latvia	0.87	0.79	0.74	0.64	0.65	0.65	75%
Lithuania	1.14	1.09	1.06	1.14	1.11	1.03	90%
Moldova	1.03	0.89	1.06	1.00	1.17	1.11	108%
Ukraine	1.69	1.76	1.94	2.21	2.40	2.30	136%
Belarus	1.27	1.17	1.25	1.12	1.18	1.04	77%

Source: International Energy Agency, *Energy Balances of Non-OECD Countries, 1996-1997*, p. II.457, (1999).

In Estonia, natural gas in particular was disproportionately consumed by industry. In 1992, 63% of total final consumption of natural gas was by industry, compared with an overall share of energy consumption by industry of 39%. The heavy industries such as chemicals accounted for a large percentage of this consumption. Natural gas accounted for 26% of non-heat energy consumption by industry. Industry consumed almost equal amounts of oil and gas, though, but because oil products were consumed much more broadly in the economy, accounted for a smaller share of oil consumption than of gas. Rising oil prices therefore disproportionately affected industry, while rising gas prices affected industry almost exclusively.<sup>6</sup> In 1992, Latvian industry was even more reliant than Estonia's on gas than on oil. Industry, iron and steel in particular, consumed 54% of Latvia's gas imports, in contrast to only 10% of its oil. Natural gas accounted for 41% of industry's non-heat energy consumption, and oil 25%.<sup>7</sup>

Lithuanian industry consumed more oil than gas. 56% of natural gas (618 toe) and 35% of oil (957 toe) were consumed by industry in 1992.<sup>8</sup> Moldovan industry consumed very little oil and petroleum products (only 41 toe or 5% of non-heat industrial consumption) and relied almost entirely on natural gas. Industry consumed 59% of Moldovan total final consumption. Gas accounted for a full 58% of non-heat industrial energy consumption.<sup>9</sup> While data for Ukraine in 1992 are incomplete, it is clear from

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<sup>6</sup> International Energy Agency, *Energy Balances and Statistics of Non-OECD Countries 1992-1993*, (1999) p. 402.

<sup>7</sup> International Energy Agency, *Energy Balances and Statistics of Non-OECD Countries 1992-1993*, (1999) p. 433.

<sup>8</sup> International Energy Agency, *Energy Balances and Statistics of Non-OECD Countries 1992-1993*, (1999) p. 437.

<sup>9</sup> International Energy Agency, *Energy Balances and Statistics of Non-OECD Countries 1992-1993*, (1999) p. 445.

1993 figures that natural gas also fueled Ukrainian industry. Industry used 55% of Ukraine's natural gas, predominantly in heavy industries such as iron, steel, chemicals and minerals. Industry also accounted for 30% of Ukraine's oil consumption. Industrial consumption of gas was 39% of Ukraine's total.<sup>10</sup> In Belarus, industry accounted for 56% of natural gas consumption and 12% of oil. Gas and oil were most heavily consumed by the chemical, machinery and construction industries.<sup>11</sup>

Table 3.6 Industrial Consumption of Natural Gas in European NIS (thousands of TJ)

	1992	1993	1994	1995	1996	1997	1997 as % of 1992
Estonia	8.7	3.9	8.1	11.9	12.2	11.9	136%
Latvia	15.2	7.2	11.1	7.7	10.1	10.0	66%
Lithuania	28.7	14.7	21.1	28.7	32.1	28.6	100%
Moldova	19.3	17.8	16.7	16.7	19.8	21.2	110%
Ukraine	1281.0	1217.0	761.8	762.8	812.6	722.0	56%
Belarus	98.5	93.7	54.5	78.9	76.0	73.2	75%

Source: International Energy Agency, *Energy Statistics of Non-OECD Countries*, 1996-1997, p. II.593. 1992 series not entirely compatible with recent years due to data reporting differences.

Energy consumption by industry in Estonia declined and allowed industrial closures and restructuring. Energy consumption began to increase again as the Estonian economy started its recovery. New, less energy-intensive industries had begun to replace the old. Industrial consumption of both natural gas and oil products exceeded 1992 levels by 1997, but this time consumption was based on world market prices and more efficient usage. Latvia followed a similar pattern, albeit one which lagged behind Estonia's. New Latvian industries placed a much greater emphasis on the use of oil, which was more

<sup>10</sup> International Energy Agency, *Energy Balances and Statistics of Non-OECD Countries 1993-1994*, (1999) p. 537.

easily imported from the West through Latvia's newly-renovated oil terminal. Thus, while natural gas consumption by industry dipped after independence and then began to climb again, as expected, consumption again began to flag as gas was replaced with oil.

All three hybrids experienced declines in industrial consumption of oil and natural gas. This is not due to growing efficiencies in their economies – quite the opposite – but rather more closely related to the shrinkage of production overall (Tables 2.2 and 3.3). All three became *less* efficient in their energy consumption since independence, and had difficulty achieving growth in their GDPs. Ukraine's drop in industrial energy consumption was the most profound (1997 industrial consumption of natural gas was just 56% of 1992 levels; oil a mere 42% of 1992 consumption) and reflected the astounding downward spiral of Ukraine's overall economy. Moldovan levels of industrial consumption of oil likewise declined (1997 levels were 60% of 1992), while industrial consumption of natural gas began to stage a modest recovery in 1994 after Moldova capitulated to Russia and the two reached a favorable pricing agreement on Russian gas exports. Lithuanian industrial consumption of oil dropped dramatically, while gas consumption fell and then began to recover, reflecting the decline of industry in Lithuania.

Belarusian industrial energy consumption changed little after independence, reflecting favorable and relatively reliable trade agreements with Russia and the relative lack of domestic industrial restructuring. Belarusian industrial consumption of natural gas dipped initially after independence, but soon climbed back to approximately 75% of

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<sup>11</sup> International Energy Agency, *Energy Balances and Statistics of Non-OECD Countries 1992-1993*,

1992 levels, where it plateaued. Industrial consumption of oil increased after independence, compensating for the drop in gas consumption, then plateaued again at approximately 1992 levels.

Table 3.7 Industrial Consumption of Oil in European NIS (1000 metric tons)

	1992	1993	1994	1995	1996	1997	1997 as % of 1992
Estonia	170	116	156	267	255	203	119%
Latvia	181	195	117	141	64	283	156%
Lithuania	976	217	208	195	185	188	19%
Moldova	40	89	33	31	28	24	60%
Ukraine	9164	6244	5172	5637	4205	3848	42%
Belarus	1507	2024	1707	1585	1444	1540	102%

Source: International Energy Agency, *Energy Statistics of Non-OECD Countries, 1996-1997*, p. II.597. 1992 series not entirely compatible with recent years due to data reporting differences.

The European NIS experienced industrial decline and sectoral restructuring in their domestic economies to varying degrees. This process – the demise of inefficient and energy-intensive heavy industry in favor of the rise of sectors that take best advantage of the comparative advantage of the country – is an essential part of the marketization of an economy and its successful engagement with globalization. It is a logical outgrowth of increases in energy prices. It is also quite hard on the industrial workers it displaces, and on the incumbent coalitions they have the power to reject. The Russophile, Belarus, experienced the least of this restructuring, maintaining relative stability and much of its old industrial base. The globalizers, Estonia and Latvia, experienced widespread industrial decline, but subsequently began to stage recoveries based in new, more efficient forms of industry and services. The hybrids also experienced overall declines in industry as well, but rather than let these industries perish,

the hybrids have struggled to keep them afloat. They have found themselves on a middle road, trying to maintain energy trade subsidies from Russia while attempting slow diversification and reform. This strategy has worked less well, and all three hybrids have been slow to realize economic recovery.

*Trade and indigenous energy resources of the European NIS*

In 1991, all six of the European NIS found themselves in the unenviable position of being large-scale energy consumers with paltry domestic energy resources. None possessed the indigenous energy capacity to meet domestic demand. All, therefore, would necessarily remain dependent upon imports. The questions facing these states were, from whom to import, and at what price. This section describes the limited energy resources of each of the European NIS and then briefly outlines their emerging energy trade patterns with Russian and the West.

Estonia had modest peat and oil shale deposits, and burned oil shale to generate the majority of its electric energy. Estonia had to import all its natural gas, oil, coal, and other energy sources. While Estonia continued to import natural gas exclusively from Russia, the relative importance of natural gas to Estonia's economy by 1998 was low, being used principally in heating and as an industrial feed stock in the chemical industry. Estonia concluded a joint ownership agreement of its gas infrastructure with Russian Gazprom, the Estonian state, and, importantly, German Ruhrgas, hoping to balance Russia's power over the Estonian gas supply. Estonia kept its accounts up-to-date with Russia, avoiding the threat of gas shut-offs on the basis of nonpayments. Unlike most

states of the former Soviet Union, by 1998 Estonia owed no energy debt to Russia. Fuel oil and gasoline were increasingly imported from Western suppliers. Only 70% of fuel oil by 1998 was imported from Russia, and renovation of the Maaruda/Muuga port was under way (and bankrolled by Western companies) to facilitate the import of crude oil and other petroleum products from non-Russian suppliers.

In 1998, Latvia still imported 90% of its energy. It possessed no coal, crude oil, or natural gas resources. Latvia did have limited (seasonal) hydroelectric, wood and peat resources, which were increasingly used in the generation of electricity. This increase in domestic energy generation helped Latvia reduce its overall dependence on imports. While Latvia remained dependent on Russia for its natural gas imports, it concluded new trade deals with German firms Ruhrgas and Preisen Electra to diversify supply and reduce Russia's power over Latvia's gas supply. Latvia achieved a sort of interdependence with Russia in the oil sector: Russia supplied Latvia oil, but needed Latvia's oil export terminal at Ventspils to export to Western markets. Latvia, in conjunction with the Scandinavian companies Neste and Statoil, began construction of an oil import terminal at Riga in order to diversify suppliers. At the same time, oil imports from non-Russian suppliers climbed since independence, accounting for 27% of oil imports by 1998.

Lithuania possessed little or no coal, crude oil or natural gas resources, and therefore necessarily relied heavily on imports. It did possess the only oil refinery in the Baltics, as well as the Ignalina nuclear power plant. Russia remained Lithuania's primary supplier of natural gas. Lithuania's oil and electric trade with Russia was more complex:

Lithuania sat between Russia and its exclave on the Baltic Sea, Kaliningrad. Lithuania's Mazeikai refinery traditionally processed oil for Kaliningrad. Unreliable Russian supplies prompted Lithuania to seek other sources, though it at first had trouble affording non-Russian imports. Non-Russian retailers, including Venezuela, were exploring the Lithuanian market. Lithuania was a net exporter of electricity (generated by the nuclear power plants, which were scheduled to be closed down), and reached a barter agreement with Russia to supply Kaliningrad with electricity in exchange for Russia's natural gas and nuclear fuel for the Ignalina reactor. While Lithuania sought some degree of energy trade diversification, it realized only limited success and continued to depend heavily on Russia.

Moldova possessed virtually no indigenous energy resources and was almost completely dependent on Russia for its imports. Moldova amassed substantial energy debt to Russia after independence. All of Moldova's gas imports were from Russia, as well as most oil imports. Moldova imported some oil from Ukraine, and a small amount from Romania. Moldova also imported its electricity from Russia and Ukraine. Moldova gained a small amount of energy trade diversification in the oil sector, but remained largely dependent on Russia.

Ukraine had substantial indigenous energy resources, though its domestic energy demand far outstripped available domestic supplies. In 1998, Ukraine filled 80% of domestic coal consumption, 23% of oil and 19% of natural gas from indigenous resources. It also possessed substantial nuclear power capacity, though these facilities unfortunately proved famously problematic. The promise of oil in the Black Sea off

Ukraine's coast may eventually help Ukraine narrow this gap between production and consumption in the future, though immense capital investment would first be necessary. While Ukraine, of our six cases, may have the greatest potential to become energy self-sufficient, that possibility remains distant. Ukraine sought to construct an interdependence with Russia in the oil and gas sectors in order to better ensure supply. Until the completion of the new Yamal pipeline, 95% of Russia's oil and gas imports to Western Europe, which earned it much-needed hard currency, transited Ukraine via the Druzhba pipeline and the Ukrainian port of Odessa. The value of this interdependence was soon undermined, however, by the Yamal pipeline, which carried Russian fuel to Europe through Belarus and Poland. Ukraine imported approximately two-thirds of its natural gas from Russia, and most of the balance from CIS member Turkmenistan. Russia was also Ukraine's primary supplier of oil, with minor imports from Kazakhstan and others. Ukraine planned to build an import terminal in Odessa to increase imports from Azerbaijan and Kazakhstan, with a goal of relying on no single supplier for more than 25% of imports, though, again, the cost of such a project has thus far proven prohibitive. While it sought diversification, Ukraine remained dependent upon Russia.

Belarus had only minor oil and natural gas deposits, and necessarily imported 90% of its energy. Russia supplied virtually all of Belarus' energy needs. Russia remained Belarus' sole supplier of natural gas. Natural gas as an energy source was more important in Belarus than in any other country of the former Soviet Union, producing 51% of all energy consumed in 1993. While Belarus benefited from preferential pricing of natural gas imports from Russia, it nonetheless maintained massive arrears to Russia

for past deliveries. Belarus also imported its oil from Russia, and in 1995 was the largest importer of Russian crude in the former Soviet Union. Belarus had two major crude oil refineries, both of which were supplied by Russian oil firms. While Belarus imported some electricity from Lithuania, the balance was either imported from Russia or generated by burning fuel oil and natural gas imported from Russia. Belarus did not seek diversification and remained almost entirely energy dependent on Russia.

Energy consumption dropped in every case since 1991, by between 34% and 51%. Imports of energy inputs fell across the board since 1991, from between 50% and 56%. This was not surprising, as contractions of the economies and energy savings in the profligate command-style economies were realized in the early years of independence. In many cases, exports did not fall as quickly as imports, as states sought revenue from transportation of Russian fuel to Western markets. Exports remained high in particular in the globalizers.

Table 3.8 Energy Balance, Estonia, 1991-1997 (toe)

	1991	1992	1993	1994	1995	1996	1997	1997 as % of 1991
Indigenous production	4810	4408	3455	3708	3464	3853	3788	79%
Import	4621	2672	2300	2733	2495	2277	2691	58%
Export	689	423	213	606	602	506	925	134%
Consumption	8742	6657	5542	5835	5357	5624	5556	64%
Net imports	3932	2249	2087	2127	1893	1771	1766	45%
Net imports as a share of consumption <sup>12</sup>	45%	34%	38%	36%	35%	31%	32%	

Source: International Energy Agency, *Energy Statistics and Balances of Non-OECD Countries, 1991-1992, 1992-1993, 1993-1994, 1994-1995, 1995-1996, and Energy Balances of Non-OECD Countries, 1996-1997*. Totals may not add because of stock changes.

<sup>12</sup> Estonia began its energy import reorientation earlier than did the other cases. Therefore, a comparison of 1997 with 1990 levels, as opposed to 1991 (as in the other cases) may be a more accurate indication of the change in energy imports from the baseline. Net energy imports as a share of energy consumption dropped by 32% between 1990 and 1997. See Statistikaamet, *Statistical Yearbook of Estonia 1999*, p 271.

Table 3.9 Energy Balance, Latvia 1991-1997 (toe)

	1991	1992	1993	1994	1995	1996	1997	1997 as % of 1991
Indigenous production	713	616	314	998	724	998	1636	229%
Import	6593	6367	4549	3727	3480	3748	2883	44%
Export	243	1083	902	205	227	314	242	100%
Consumption	7063	5900	3961	4520	3977	4432	4460	63%
Net Imports	6350	5284	3647	3522	3253	3434	2641	42%
Net imports as a share of consumption	90%	90%	92%	78%	82%	77%	59%	

Source: International Energy Agency, *Energy Statistics and Balances of Non-OECD Countries, 1991-1992, 1992-1993, 1993-1994, 1994-1995, 1995-1996, and Energy Balances of Non-OECD Countries, 1996-1997*. Totals may not add because of stock changes.

Perhaps more interesting is the share of net imports (thus discounting throughput) as a percentage of consumption. This measure may serve as an indicator of the extent to which the state had successfully used conservation, or increased efficiency in the use of energy, and increased domestic production, in order to address the problems of energy imports. Net imports as a share of consumption indicate the extent to which the domestic energy sector is dependent on trade.

Table 3.10 Energy Balance, Lithuania 1991-1997 (toe)

	1991	1992	1993	1994	1995	1996	1997	1997 as % of 1991
Indigenous production	4478	3932	3394	2454	3554	4168	3970	89%
Imports	18489	8911	9585	8024	8036	8263	9118	49%
Exports	5120	2254	4434	2816	2460	3362	4178	82%
Consumption	17847	10589	8545	7662	9130	9069	8806	49%
Net imports	13369	6657	5151	5208	5576	4901	4940	37%
Net imports as a share of consumption	75%	63%	60%	68%	61%	54%	56%	

Source: International Energy Agency, *Energy Statistics and Balances of Non-OECD Countries, 1991-1992, 1992-1993, 1993-1994, 1994-1995, 1995-1996, and Energy Balances of Non-OECD Countries, 1996-1997*. Totals may not add because of stock changes.

Table 3.11 Energy Balance, Moldova 1991-1997 (toe)

	1991	1992	1993	1994	1995	1996	1997	1997 as % of 1991
Indigenous production	30	22	32	54	48	53	96	241%
Imports	8724	7429	5482	4699	4423	4401	4440	59%
Exports	482	485	3	0	11	0	2	0.4%
Net imports	8242	6944	5479	4699	4412	4401	4438	54%
Consumption	8272	6966	5511	4753	4460	4454	4436	54%
Net imports as a share of consumption	100%	100%	99%	99%	99%	99%	100%	

Source: International Energy Agency, *Energy Statistics and Balances of Non-OECD Countries, 1991-1992, 1992-1993, 1993-1994, 1994-1995, 1995-1996, and Energy Balances of Non-OECD Countries, 1996-1997*. Totals may not add because of stock changes.

Table 3.12 Energy Balance, Ukraine 1991-1997 (toe)

	1991	1992	1993	1994	1995	1996	1997	1997 as % of 1991
Indigenous production	114470	115577	99310	86596	80959	79042	81175	71%
Imports	146039	121984	94029	80488	84686	77357	73701	50%
Exports	13514	9577	4095	5192	3800	2463	4818	36%
Consumption	246995	227984	189244	161892	161845	153936	150059	61%
Net imports	132525	112407	89934	75296	80886	74894	68883	52%
Net imports as a share of consumption	54%	49%	48%	47%	50%	49%	46%	

Source: International Energy Agency, *Energy Statistics and Balances of Non-OECD Countries, 1991-1992, 1992-1993, 1993-1994, 1994-1995, 1995-1996, and Energy Balances of Non-OECD Countries, 1996-1997*. Totals may not add because of stock changes.

The globalizers displayed the greatest progress in reducing dependence on imports. By 1997, Estonia had reduced its dependence by 32% and Latvia by 35%. Lithuania and Ukraine also managed to reduce their dependence on energy inputs. Lithuania's net imports as a share of consumption dropped by 25% between 1991 and 1997, while Ukraine's fell 15% between 1991 and 1997. The other states experienced virtually no change in their degree of energy dependence (a two-point change in Belarus,

and no change in Moldova), remaining almost entirely dependent on energy imports from abroad.

Table 3.13 Energy Balance, Belarus 1991-1997 (toe)

	1991	1992	1993	1994	1995	1996	1997	1997 as % of 1991
Indigenous production	3963	3482	2818	3141	3313	3147	3275	83%
Imports	51489	38592	27522	25424	24505	24149	25705	50%
Exports	13311	5029	1603	3039	3425	4223	3371	25%
Consumption	42141	37045	28737	25526	24393	23073	25142	66%
Net imports	38178	33563	25919	22385	21080	19926	22334	58%
Net imports as a share of consumption	91%	91%	90%	88%	86%	86%	89%	

Source: International Energy Agency, *Energy Statistics and Balances of Non-OECD Countries, 1991-1992, 1992-1993, 1993-1994, 1994-1995, 1995-1996, and Energy Balances of Non-OECD Countries, 1996-1997*. Totals may not add because of stock changes.

Table 3.14 Summary of Energy Resources and Trade Policy toward Russia

Country	Indigenous Energy Resources Relative to Consumption	Energy Trade Strategy
Estonia	low: oil shale, peat	Westward diversification
Latvia	negligible (but increasing): hydro, wood, peat	Westward diversification
Lithuania	low: nuclear	Continued dependence on Russia, limited diversification
Moldova	negligible	Continued dependence on Russia, limited diversification
Ukraine	low: coal, nuclear, oil and gas	Continued dependence on Russia, limited diversification
Belarus	negligible: minor oil and gas	Russian orientation

As expected, dependence on energy imports was not a sound indicator of energy trade diversification. Estonia and Ukraine, which in 1991 began with comparable levels

of trade dependence, diversified import sources and develop indigenous resources at very different rates, Estonia being swiftest of the cases and Ukraine making little progress whatsoever. Latvia, Moldova, and Belarus also began with comparable levels of energy trade dependence, but emerged with completely divergent energy trade strategies.

#### **IV. Conclusion**

The greatest decreases in energy dependence on Russia were achieved in the globalizers, where pro-internationalist coalitions dominated the state and were able to implement consistent reformist policies. These coalitions were held in place, at least in part, through the political exclusion of those sectors most injured by rising prices on natural gas and oil, that is industry. This exclusion took the form of discriminatory language laws. By contrast, Belarus, the Russophile, embraced its energy dependence, and sought to maintain its energy subsidies in order to avoid sectoral restructuring. It remained almost entirely dependent upon Russia for its energy. The hybrids were dominated by fragmentation and alternating left and center coalitions, and sought both energy trade diversification and the maintenance of Russian energy subsidies. They met with less success than either the globalizers or the Russophile. The following chapters describe in greater detail the cases of the globalizers, hybrids, and Russophile.

## **CHAPTER IV**

### **ENGAGING GLOBALIZATION: ESTONIA AND LATVIA**

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#### **I. Summary**

The globalizers. Estonia and Latvia. have pursued policies of liberalization, energy trade reorientation. and opening to the international market. These policies have been executed by the rule of right and center-right, pro-market, pro-West reformist coalitions. The maintenance of power of these coalitions through the difficult economic times brought on by the liberalizing policies has been facilitated by the exclusion of those most ill-affected by these policies, the resident Russophones of the industrial sector, through their political disenfranchisement. The globalizers have made significant headway in reducing their vulnerability to Russian energy stoppages and in increasing the security of their energy supplies. Both globalizers have pursued a pro-Western foreign policy, seeking both EU and NATO membership. They have met with greater success than their neighboring Baltic state, Lithuania: both Estonia and Latvia are now on the short list of countries to be included in the next wave of EU expansion.

Estonia has most clearly, and most effectively, embraced the strategy of globalization. It has made the most progress toward engagement of the global economy. While Russia is now and will remain an important economic associate, Estonia's primary trading partners are in Western and Northern Europe. The level of foreign investment Estonia received since independence is virtually unprecedented in the post-Soviet world. Estonia experienced the most dramatic and earliest energy trade reorientation of all cases.

Estonia has been most successful in maintaining a pro-reform, pro-Western government with liberal economic and trade policies. Estonia also experienced some of the most dramatic political disenfranchisement of those worst affected by energy trade reorientation and the changes in prices and industrial restructuring such a reorientation necessitates. The exclusion from citizenship and denial of federal voting rights of non-Estonian speakers has had the most dramatic effect in the northeastern regions, which are heavily populated by ethnic Russians. These regions were also the center of heavy industry, which suffered greatly from the decline in energy subsidies which energy trade reorientation produced.

Latvia has likewise pursued a strategy of globalization, albeit at a somewhat slower pace. I argue that, while Latvia experienced many changes of government since independence, these governments were pro-internationalist, pro-market reform, and anti-Russian, enabling Latvia to maintain a relatively consistent strategy as a globalizer and to decrease its dependence on Russian energy subsidies. As in Estonia, the maintenance of this pro-internationalist coalition was facilitated by the exclusion of Russophone residents from the electoral process.

In this chapter I will argue that Estonia and Latvia's choice of globalization, and success in pursuing this goal, were fundamentally built on the exclusion from national politics of the segments of society which would suffer worst under these policies. The Russian-speaking minority was denied citizenship, and thereby the right to vote in national elections. These residents tended to be more pro-Russia and pro-socialist than their Estonian- or Latvian-speaking counterparts. They also populated the economic

sectors and regions that suffered most under liberalization and energy trade reorientation. Their exclusion from politics helped to ensure the consistency of rightist, liberal, pro-Western policies, which was essential to the success of Estonia and Latvia's energy trade reorientation and embrace of the globalization process.

The globalizers meet both the conditions of the globalizer model. Both possessed relatively less mobilized and organized ethnic minorities concentrated in the economically vulnerable sectors. This facilitated the second condition, domination by globalist coalitions. Estonia was ruled consistently since independence by reformist, pro-internationalist, anti-Russian coalitions. Latvia's ethnic minorities were somewhat less concentrated than were Estonia's, and therefore its ruling coalitions were slightly less consistently globalist: Latvia experiences a slight shift to the center-right from the far-right in 1995-1997. It is not surprising then that Latvia had lagged behind Estonia somewhat in energy trade reorientation and liberalization. Nevertheless, both were clearly globalizers.

In Part II, I outline the history and demography of Estonia. I argue that, because of Estonia's history in both the "East" and "West," Estonia's current strategy as a globalizer was not culturally predetermined. I also explain the origins of Estonia's Russian minority and the political, regional and economic differences between this minority and the titular majority. I then turn to the history of Estonia's post-Soviet ruling coalitions, and argue that the exclusion of the Russian population from national elections has helped to ensure the continued rule of right-wing reformist coalitions. Using electoral data, I demonstrate the difference in electoral outcomes when Russian-speakers are

excluded from the electorate. I then outline the consequences of these coalitions for foreign, economic and energy policies. I then outline more briefly the secondary globalizer case of Latvia.

## **II. History and Nation: Estonia and the East-West Divide**

### *History*

Estonia is a small country of 17 thousand square miles and 1.4 million people, located at the far northeastern corner of the chilly Baltic Sea. It borders Latvia to the south and Russia to the East, and just 50 miles off its lengthy coast sits Finland. Approximately 65% of Estonia's population is ethnic Estonian, 25% Russian, 4% Ukrainian and Byelorussian. Estonians are predominantly Lutheran, with Russian Orthodox, Baptist and Roman Catholic minorities. Estonian, the state language, is a member of the small Finno-Ugric language group. It is most closely related to Finnish, and a distant cousin of Hungarian, the only other significant living language of the family. Its principal natural resources consist of forests, fisheries, and, in the energy sector, oil shale and peat.

Estonia has a long history of imperial occupation. During this history, Estonia was exposed to the cultures of the East and West under Russian, Baltic and Scandinavian rule. Estonia was ruled by the Livonian Teutonic Knights for the greater part of the thirteenth through fifteenth centuries. It was then ruled by Sweden until Sweden's defeat by Peter the Great in 1721, when Estonia became a subject of the Russian Empire. Under the tsars, Estonia experienced its first wave of Russification, as Russians emigrated

westward. Around the time of the Revolution in 1917, Russia granted Estonia local autonomy, and in 1918 Estonia declared independence. Estonia was briefly occupied by Germany in 1918-1919, after which it experienced its 20-year period of independence. Estonia was politically sovereign during the inter-war period, roughly from 1919 to 1940. Despite some difficulties, Estonia eventually established for a time during this period a democratically-elected presidency and parliament. World events cut short Estonian independence, however. In 1939, Estonia was forced to accept the presence of Soviet military bases on its territory, and in 1940 was incorporated into the Soviet Union under the secret protocol of the German-Soviet nonaggression pact of 1939. Estonia again suffered German occupation from 1941-1945, and was reincorporated into the Soviet Union after the war. It was not until 1989 that the Estonian Supreme Soviet unilaterally annulled the annexation and began the struggle for the reassertion of independence.

The intervening 49 years, however, had a dramatic impact on the development of Estonia's economy and society. The bulk of industrialization in Estonia took place in the post-war period, under Soviet rule, according to communist logic -- such as it was. As in most of the rest of the Soviet Union, industry in Estonia was built on the model of gigantism, favoring heavy industry, and with little regard to the efficient use of energy resources. A second, larger wave of Russification also took place as Russians were relocated to Estonia to fill its burgeoning factories and industry. The industrialization of Estonia also served two other purposes: the Russification of the population and the fostering of Estonian economic dependence on Russia for fuel imports.

*Political enfranchisement and language laws*

Russian communities have long existed in Estonia. The earliest recorded communities may be those established by Yaroslav the Wise, who founded the town of Yuryev (Tartu) in 1030. Fourteenth century documents mention the existence of Russian villages in Eastern Estonia. However, the share of Russians in the Estonian population before the 18<sup>th</sup> century is estimated to be very low, perhaps 1%. While Peter the Great took Estonia from Sweden in 1721, Russification did not begin in earnest until the 19<sup>th</sup> century. At the end of the 1830s, construction of Russian orthodox churches began in eastern Estonia in order to encourage the immigration of Old Believers out of Russia. In addition, Russian missionaries began to arrive and an Estonian diocese was established. According to population censuses, the Russian population of Estonia roughly doubled between 1867 and 1881. Tsar Alexander III, crowned in 1881, abolished the special status of the Baltic region and proclaimed Russian the official language. This led to an influx of Russian teachers, civil servants and immigrants of all sorts. The Russian population continued to increase as railroads were built between Russia and Estonia, and the Russian port in Tallinn grew. By 1922, approximately 8.2% of the Estonian population were Russians.

More dramatic demographic changes took place during the Soviet occupation of Estonia. As in its neighboring republics, in Estonia, large numbers of the Baltic peoples were murdered or forcibly deported to Siberia and elsewhere, while at the same time thousands of Russians were relocated to the Baltic republics. Prior to World War II, 90% of the residents of Estonia belonged to the titular majority. In stark contrast, by 1991,

only 65% of people living in Estonia were ethnic Estonians. The Soviet authorities remade the face of Estonian demographics in only a few decades.

Contemporary Estonia has a very large Russian-speaking minority. As of 1999, the population of Estonia was approximately 1.4 million and was comprised of 65% ethnic Estonians, 28% Russians, 2% Ukrainians, and 1% each Byelorussians and Finns.<sup>1</sup> Estonia has implemented citizenship laws that required residents who could not prove descent from pre-1940 Estonian residents to pass language tests in order to be eligible to vote in national elections. While the Estonian language is generally agreed to be melodic and pleasing to the ear, it also possesses a very complex grammar and is notoriously difficult to learn. The Baltic states view the events of 1991 as the reassertion of the independence they enjoyed in the inter-war period, and assert that there is a continuity between the political entities that existed prior to the Soviet invasion and those that now exist after its collapse. After independence was reasserted in 1991, the legislature of Estonia decided that only people who could prove that they or their ancestors were citizens of Estonia before the Soviet takeover in 1940 would be granted automatic citizenship, regardless of ethnic heritage. The result of this law was that only about 100,000 of the approximately 550,000 Russian-speakers living in Estonia in 1991 were granted automatic citizenship.

This political exclusion meant that the majority of the Russian-speaking populations did not have a voice in national policy. In 1992 in Estonia, for example, the constitution was adopted by popular referendum and parliamentary elections were held.

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<sup>1</sup> Central Intelligence Agency, *World Factbook*, 1999.

In a country where nearly a third of the residents were Russian speakers, not a single ethnic Russian was elected to the 101-seat Riigikogu (national legislature). Naturalization procedures were eventually set in place. Strict language requirements made a written and oral command of the titular language a necessity for naturalization. Under the Soviet system, almost all Soviet citizens learned Russian but few Russians were required to learn local languages.

The political rights of non-citizen residents in Estonia were quite limited. While in Estonia resident non-citizens could vote in local elections only, resident non-citizens could not hold elected office of any sort. The requirements for residency permits themselves were quite contentious. For example, in 1993 Estonia passed the Law on Aliens which required, among other things, that all residents apply for permits no matter how long they had lived in Estonia, and did not guarantee that the applications would be approved. This caused dissatisfaction among the Russian-speaking population and sparked a brief secessionist movement in the Russian-populated northeast regions of Estonia. The rules on permits were eventually softened.

These so-called "language laws" came under some criticism as being discriminatory, particularly because many of the non-citizens had lived in these countries for most, if not all, of their lives. Many non-citizens argued that they were not immigrants: they did not change states, the states around them changed. Therefore, they should not be required to apply for citizenship. Advocates of these laws have defended them on many bases, including the language proficiency many countries, including the United States, require of their immigrants. In addition, there is the argument that

linguistically heterogeneous societies undermine civic unity, and that a common language may make a society more cohesive and a country more stable and easier to govern.

*Regional consequences of citizenship laws*

Whatever the reasoning behind these laws, they had profound consequences for the politics and economics of Estonia. The geographical and economic distribution of Russian speakers in Estonia was of considerable importance. The Russian population of Estonia was to be found mainly in urban areas, while the rural areas were mainly populated by the titular majorities. A full 92% of ethnic Russians in Estonia lived in urban areas compared with the national average of 70%. In Tallinn, the capital of Estonia itself, Russian-speakers comprised 50% of the population.

In Estonia, regional distribution of the Russian-speaking minority was quite dramatic. The population of the northeastern regions of Estonia, which include the cities of Narva, Sillamae and Kohtla-Jarve, was mostly Russian-speaking. In these cities, Russian-speakers comprised more than 95% of the population. These northeastern regions and cities were also the heart of Estonian heavy industry. The regions of Ida-Viru, in the far northeast of the country, and Harju, in which the city of Tallinn is found, were the most densely-populated by Russian-speakers. These regions contained the highest proportion of ethnic Russians and other Slavic peoples, whose language is commonly Russian.

Harju and Ida-Viru counties experienced the largest net out-migration since independence. The largest wave of migration took place in 1992, immediately after

independence was realized.<sup>2</sup> Most of this migration was of Russian-speakers moving to Russia. Estonia's population stabilized in subsequent years, however. Ethnic proportions in Estonia and in individual regions remained largely stable since 1995, the earliest year for which these data were available. Therefore only 1999 data are included here. It is interesting to note that the concentration of ethnic Russians in Ida-Viru and Harju would be even higher had more Russians felt secure enough to stay in post-Soviet Estonia.

Table 4.1 Ethnic Population in Estonia, by County, January 1, 1999

<b>County</b>	<b>Estonians</b>	<b>Russians</b>	<b>All Slavs<sup>3</sup></b>
Ida-Viru	19%	71%	77%
Harju	54%	36%	42%
Tartu	79%	17%	19%
Valga	78%	15%	18%
Laane-Viru	81%	14%	17%
Laane	84%	12%	15%
Parnu	84%	11%	14%
Jogeva	89%	9%	10%
Polva	94%	5%	6%
Rapla	91%	5%	6%
Viljandi	92%	5%	6%
Jarva	92%	4%	5%
Voru	94%	5%	5%
Hiiu	96%	2%	3%
Saare	97%	2%	2%
<b>ESTONIA</b>	<b>65%</b>	<b>28%</b>	<b>32%</b>

Source: Statistikaamet, Statistical Office of Estonia, Endla 15, 15174 Tallinn, Estonia, 1999.

While ethnicity is a good indicator of linguistic ability in Estonia, it is of course imperfect. It is therefore helpful to turn to other indicators of predominant language, such

as the language of instruction in schools. In Harju county, for example, 41% of children in school had to be taught in Russian, and 46% in the city of Tallinn itself, compared to the national average of 29%. In Ida-Viru county, a full 83% of students were taught in Russian. This stands in stark contrast to Tartu and Valga counties, where 15% of students were taught in Russian. In Lanne-Viru and Parnu counties, this percentage was 11%, and in Lanne and Jogevea counties, it was between 6 and 7%. In the remaining 7 counties -- Jarva, Voru, Polva, Viljandi, Rapla, Hiiu, and Saare -- virtually no classes, between 0-3%, were conducted in Russian.<sup>4</sup> These rates correlate well with the ethnic population data, confirming that Russian speakers comprised the vast majority of the population in Ida-Viru county and near parity in Harju county. Russian-speakers constituted a substantial minority in six other counties. The remaining seven counties were populated almost exclusively by Estonian-speakers.

Post-independence economic policy had different effects in different regions. The Russian-speaking regions were particularly hard-hit. Unemployment in particular has been a problem, at 30% by some estimates in Narva. Higher unemployment rates among Russians were due to the fact that it was mostly they who worked in the heavy industry and transportation sectors that all but closed down after 1991. These unemployment rates gave rise to social problems such as increased drug and alcohol abuse and crime.<sup>5</sup>

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<sup>2</sup> Statistikaamet, *Regional Statistics 1998*, pp. 54-55.

<sup>3</sup> Includes Russians, Ukrainians and Belorussians.

<sup>4</sup> Ibid., p 62.

<sup>5</sup> Interview with author, Leivi Sher, Advisor, United People's Party of Estonia Faction, Estonian Parliament, October 19, 1999.

*Differences between Estonian- and Russian-speakers*

The Estonian-speaking and non-Estonian speaking populations differed greatly. The Estonians were generally better educated and in a better position to take advantage of the market economy. According to a poll conducted the Open Estonia Foundation, 48% of those with Estonian citizenship were employed as managers or specialists of some sort, while only 21% of those with Russian citizenship were. These populations also differed substantially in their view of Estonia's foreign policy priorities. While only 34% of those with Estonian citizenship considered Russia to be a safe neighbor, 53% of those with Russian citizenship and 42% without citizenship considered Russia to be a safe neighbor. Likewise, 60% of Estonian citizens were in favor of Estonia's accession into the European Union, while only 43% of Russian citizens and 53% of stateless residents agreed. Non-Estonian citizens also tended to have a more leftist view of economic policy. This was reflected perhaps in their view of the European Union, but also in their view of the Soviet era. A full 70% of Estonian citizens with Russian citizenship prefer Soviet-era Estonia.<sup>6</sup>

In Estonia, the economic "losers" under energy reorientation were old energy-intensive heavy industries. These industries were concentrated in the Russian-populated eastern regions of Estonia. The northeast counties of Estonia were most reliant on manufacturing and the generation of electricity, even long after independence and energy trade reorientation.<sup>7</sup> The economic contraction following independence was most severe

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<sup>6</sup> "Principal Differences Between Non-Estonians With Estonian Citizenship or Without Citizenship and Those With Russian Citizenship", Open Estonia Foundation, 1997.

<sup>7</sup> Statistikaamet, *Regional Statistics 1998*, p. 258.

in these regions. The economies of these regions were also the slowest to recover. Benefiting from the new Estonian economy were the new service sector, new light industries, and export-oriented businesses.

### **III. Political Coalitions: Right-Wing Reformist Consensus**

Election data demonstrate marked differences between the Russian-populated and Estonian-populated regions of Estonia. The Russian-speaking population was more left-leaning (pro-communist and pro-socialist) and pro-Russia (and Pro-Soviet Union) than their Estonian-speaking neighbors. The virtually total exclusion of the Russian-speaking populations from national politics in the independence-era Estonia gave the national government considerable leeway in economic, energy and foreign policy. As one analyst of Estonian elections noted in 1996, "If the supporters of the [Russian] Empire were given the right to make decisions concerning Estonia's independence (in a democratic way, by giving everybody living in Estonia the right to vote). Estonia would soon again be part to the Russian Empire."<sup>8</sup> Even if this is something of an overstatement, it seems clear that the political disenfranchisement of the Russian-speaking population afforded the Estonian government the ability to maintain pro-market, right-wing governments and anti-Russian policies and reforms despite the costs these policies imposed on the

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<sup>8</sup> Tiina Raitviir, *Eesti Uleminekuperioodi Valimiste (1989-1993) Vordlev Uurimine (Elections in Estonia During the Transition Period: A Comparative Study (1989-1993))*, (Estonian Academy of Sciences: Tallinn, 1996), p. 382.

population. The exclusion of Russophones produced more reformist, right-wing outcomes than in elections in which Russian-speakers were included.

In this section I first outline the impact of the exclusion of Russophones on national politics. By the contrasting results of inclusive and exclusive elections, I show how the exclusion of Russophones, and thus the bulk of workers in the heavily-industrialized regions, allowed for the election and maintenance of reformist, right-wing governments and coalitions. I then outline the election and composition of the ruling coalitions in Estonia. A right-wing reformist parliament was elected in 1992, and in turn chose a right-wing reformist president. Following difficult economic times and the extension of citizenship to a small number of Russian residents, in 1995, parliamentary elections yielded an ostensibly more centrist right-wing reformist parliament. The new parliament chose to reelect the same president as the old, and pursued the same energy and macroeconomic policies as the previous government. Reformist, right-wing coalitions were thus maintained.

#### *Elections of the transition period: late Soviet elections*

National elections were held in 1989 and 1990, while Estonia was still the Estonian Soviet Socialist Republic. While aspects of these elections may certainly not be considered free and fair by international standards, political reforms had been introduced under the Gorbachev regime which enabled a greater degree of choice and electoral competition than ever before. For this reason, the results are relevant to this study and will be included here.

Mass support for Estonian independence began in the summer of 1988, in what came to be known as the “singing revolution.” In November of that year, the Estonian SSR adopted the “Declaration about Sovereignty.” The issues that grew out of this declaration, of economic independence and political sovereignty, in addition to questions of citizenship and official language, became the central issues in the elections to the USSR Congress of People’s Deputies the following year. In March 1989, elections to the Congress of USSR People’s Deputies were held in Estonia.<sup>9</sup> The result was the election of 33 deputies to be sent to the federal body in Moscow. Twenty-seven of these deputies were openly pro-independence, and made their voices heard to that effect in Moscow. The remaining six deputies were conservatives, advocating the preservation of the Soviet Union. These conservatives were elected from the regions in Estonia which were populated heavily by Russian-speakers and the economies of which were based in military and heavy industry.<sup>10</sup>

Two important elections took place nearly simultaneously in January and February of the following year: those to the Estonian Supreme Council and to the Estonian Congress. While still under the auspices of the Soviet Union, elections to the Estonian Supreme Soviet included nine registered parties or popular movements, in addition to independent candidates. The elections produced the first functioning parliament of the

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<sup>9</sup> These elections were held within the context of Soviet institutions and were inclusive in the sense that anyone over the age of 18 was eligible to vote, regardless of ethnic origin or linguistic ability. The most nationalistic groups in Estonia declined to participate in the elections within the Soviet context, fearing participation would be seen as legitimating further Soviet occupation.

<sup>10</sup> Tiina Raitviir, *Eesti Uleminekuperioodi Valimiste (1989-1993) Vordlev Uurimine (Elections in Estonia During the Transition Period: A Comparative Study (1989-1993))*, (Estonian Academy of Sciences: Tallinn, 1996) and Estonian National Electoral Committee, “Elections and Referendums in Estonia, 1989-1999”, 1999.

soon-to-be independent Estonia. Voting rules were again inclusive, giving the right to vote to all residents over the age of eighteen.

Elections to the Estonian Congress were quite different. First, the Estonian Congress was an unofficial congress, and was not intended to serve as a permanent legislative body.<sup>11</sup> Instead, the elections were set up explicitly as an alternative to the Soviet elections, by pro-nationalist groups within Estonia. "Estonian Citizens' Committees" were established throughout the country for the purpose of preparing for the elections. All post-1940 immigrants were excluded from participation, ensuring that votes were cast by Estonian nationals only. These were to be the first, but not the last, exclusive elections held in Estonia.

The differences between the results of these two nearly simultaneous elections – one inclusive, one exclusive – demonstrate the importance disenfranchisement of Russian-speakers to national politics. Estonian Congress elections, in which only Estonians were allowed to vote, produced a right-wing body, which was virtually unanimously pro-independence, pro-liberal economic reform, pro-Western, and anti-Soviet. By contrast, the Estonian Supreme Council, in which all residents were permitted to vote, produced a more mixed body, with results varying according to region. While the election was an overall victory for the Popular Front, a center-right pro-independence group which won 43 seats, Communist and pro-Russian candidates each took approximately 27 seats. A Popular Front government was formed. The Moscow-

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<sup>11</sup> The Estonian Congress did come to possess considerable power, however, when the Estonian Supreme Council declared restoration of independence on August 20, 1991, and joined with the Estonian Congress to form a Constitutional Assembly.

friendly candidates were most often supported by the Russian-speaking electorate. Cities such as Narva and Sillamae, heavily industrial and Russian-speaking, elected exclusively leftist and pro-Moscow candidates. Such regional differences were absent in the Estonian Congress elections because these Russian-speaking industrial workers were excluded from voting.

### *Referenda*

Two referenda were held early in the transition period, again, one inclusive and one exclusive; again, the exclusion of Russian-speakers had a profound impact on the outcome. A referendum on independence took place on March 3, 1991. All residents, regardless of nationality, were allowed to participate. 78% of voters<sup>12</sup> cast their ballots in favor of independence from the Soviet Union. This implies that some Russian-speakers at least voted in favor of independence. However, clear trends emerge from regional voting patterns: the heavily-industrialized Russian-speaking areas voted more strongly against independence, while the rest of Estonia voted strongly in favor of it. Only in the industrial, Russian-populated cities of Narva, Tallinn, and Kohtla-Jarve did more than 30% of the electorate vote for remaining in the Soviet Union.<sup>13</sup> In Tallinn, 33%, in Kohtla-Jarve, 52%, and in Narva, 73% of voters cast their ballots against independence.<sup>14</sup>

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<sup>12</sup> Estonian National Electoral Committee, "Elections and Referendums in Estonia, 1989-1999", 1999.

<sup>13</sup> Ibid.

<sup>14</sup> Tiina Raitviir, *Eesti Uleminekuperioodi Valimiste (1989-1993) Vordlev Uurimine (Elections in Estonia During the Transition Period: A Comparative Study (1989-1993))*, (Estonian Academy of Sciences: Tallinn, 1996), p. 381.

The highest percentage of “no” votes by county were in Ida-Virumaa (18%), Harjumaa (13%), and Valgamaa (11%), and Laane-Virumaa (8%).<sup>15</sup>

A second referendum on the acceptance of the new constitution was held in June of 1992. Unlike in the first referendum, non-Estonians were excluded from voting. The draft constitution was overwhelmingly approved by 91% of voters. Some regional differences could be observed, but they were much smaller than in the previous referendum. Rejection of the constitution was most often by the fundamentalists of the far right, not the far left.<sup>16</sup> An additional question was also included on the ballot, asking if those who had applied for Estonian citizenship before June 5<sup>th</sup> 1992 should be allowed to participate in the first post-independence parliamentary and presidential elections. This was the first time the question of voter exclusion had been put directly to the Estonian voters, and 53% of them voted in favor of it. Again, regional variation was less dramatic than in the inclusive referendum.

### *Local elections*

In the independence period after the referenda, it was established that non-Estonian speakers, that is, “non-citizens”, would not be permitted to participate in national elections. However, permanent residents of more than five years would be allowed to vote, though not run for office, in local elections. The differences in outcomes of these elections may be taken as an indication of how national electoral outcomes

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<sup>15</sup> Ibid., p. 443.

<sup>16</sup> Ibid., p. 350.

would have differed had Russian-speakers been allowed to participate. I will also consider the last round of Soviet-era local elections.

Elections to Local Councils of People's Deputies took place in the late Soviet period, in December 1989. A 5-year residency requirement was placed on voter eligibility. However, after strikes in the factories of Tallinn and other areas with large Russian-speaking populations took place, this requirement was dropped.<sup>17</sup> The Popular Front did well, as did the Communist Party. Some pro-Soviet Russians still chose to boycott the elections out of protest. Regional trends were quite clear, however: areas heavily populated with Estonians elected pro-independence, right-wing parties, while areas populated by Russian-speakers, particularly heavily industrialized regions like the north east, favored pro-Soviet Union candidates. The exception to this was the heavily Russified Tallinn, where the Russian boycott was strongest, resulting in the election of pro-independence local governments.<sup>18</sup>

Local council elections were held again in 1993, with similar regional patterns. A 5-year residency requirement for voters was put in place this time. The right-wing Pro Patria party did well overall.<sup>19</sup> However, pro-Soviet Union parties did well in Russian-speaking areas, particularly in the industrialized northeast, and particularly in urban areas. The northeastern cities of Narva, Sillamae and Kohtla-Jarve remained the stronghold of

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<sup>17</sup> Estonian National Electoral Committee, "Elections and Referendums in Estonia, 1989-1999," 1999.

<sup>18</sup> Tiina Raitviir, *Eesti Uleminekuperioodi Valimiste (1989-1993) Vordlev Uurimine (Elections in Estonia During the Transition Period: A Comparative Study (1989-1993))*, (Estonian Academy of Sciences: Tallinn, 1996), p. 352.

<sup>19</sup> Estonian National Electoral Committee, "Elections and Referendums in Estonia, 1989-1999," 1999.

supporters of closer relations with Russia, along with the capital, Tallinn.<sup>20</sup> Leftists and left-centrists were elected most often in Tallinn, industrialized centers and the northern towns. These areas are again those with the highest proportion of Russian-speakers.<sup>21</sup>

### *National elections*

Estonian parliamentary elections took place in 1992 and 1995.<sup>22</sup> Presidential elections were held in 1992 and 1996 (the second indirectly, by parliament). Only Estonian citizens were allowed to vote in these, a prerequisite of citizenship being proficiency in the Estonian language. The 1992 elections produced a right-wing coalition in government, led by the Pro Patria party and Prime Minister Laar. Regional trends were less pronounced than in the local elections. Tallinn and Tartu were right-centrist, while towns in the northeast and Ida-Virumaa were left-centrist.<sup>23</sup> The fact that Estonian-speaking workers in the industrialized northeast voted left-centrist is perhaps not surprising, given that their livelihoods depended on the same heavy industry as their Russian-speaking neighbors. However, since the number of Estonian-speaking voters in these regions was very small, their impact on national elections was negligible.

At the same time, direct elections for the Presidency were held for the first and last time. (The president was hereafter to be elected by the parliament.) Four candidates

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<sup>20</sup> Tiina Raitviir, *Eesti Uleminekuperioodi Valimiste (1989-1993) Vordlev Uurimine (Elections in Estonia During the Transition Period: A Comparative Study (1989-1993))*, (Estonian Academy of Sciences: Tallinn, 1996), pp. 383-384.

<sup>21</sup> *Ibid.*, pp. 352-353.

<sup>22</sup> Parliamentary elections were held again in 1999, resulting in a swing back to the far right.

<sup>23</sup> Tiina Raitviir, *Eesti Uleminekuperioodi Valimiste (1989-1993) Vordlev Uurimine (Elections in Estonia During the Transition Period: A Comparative Study (1989-1993))*, (Estonian Academy of Sciences: Tallinn, 1996), p. 355.

ran. Arnold Ruutel, a former high Communist Party functionary and current Chairman of the Presidium of the Supreme Council, won 42% of the popular vote. Lennart Meri, a well-known author and Ambassador to Finland, received 29%. Since no single candidate received a clear majority, parliament voted between the two front-runners. The Parliament chose the right-wing candidate Meri over the left-wing Ruutel by a 59:31 vote.<sup>24</sup>

Parliamentary elections were held again in 1995. By that time, a small number of Russian residents had become citizens. The Estonian economy had also suffered some very difficult times. The elections resulted in a move from the far right of the previous government to the center-right of the new. For the first time, some Russians were represented in the legislature. The rural Coalition Party and Rural Union, led by Tiit Vahi, formed a government with the Estonian Center Party. These had been the main “opposition” in the previous parliament. The Pro Patria, Estonian National Independence Party and the so-called Moderates, who had formed the government in the previous parliament, became the new opposition.<sup>25</sup> It is important not to overstate the magnitude of this political shift. There was broad consensus and continuity of policy among the major parties on the issues of Estonian independence, relations with Russia, engagement with Western Europe, and especially the advancement of liberal economic reforms.<sup>26</sup> Indeed, in 1996, the new parliament re-elected the same right-wing President Meri who had been out in place by the previous “opposition” government.

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<sup>24</sup> Ibid., pp. 358-359.

<sup>25</sup> Estonian National Electoral Committee, “Elections and Referendums in Estonia, 1989-1999,” 1999.

When inclusive elections were held in Estonia, the results were more left-wing, pro-Russian, and pro-Soviet Union. Moreover, these left-wing, pro-Russian, candidates were generally elected in the heavily industrialized, Russian-populated regions. Not surprisingly, when most of the voters in these regions were excluded from voting, the results of elections were more right-wing, anti-Russian and anti-Soviet Union. This electoral exclusion was instrumental in allowing the Estonian state to maintain a right-leaning, pro-Western, pro-liberal national legislature and right-wing, pro-Western, liberal policies.

The exclusion of many Russian-speakers from participation in national elections helped to maintain the right-wing governments. Among the Russian population, there is a call for more centrist or leftist policies:

In most European states, there is a sharing of power between right and left. [Because it is not so in Estonia,] our economic policy is not in balance. The economy and the society must be in balance. We do not have such a balance.<sup>27</sup>

#### **IV. Policy: Engaging Globalization**

Of the three states, Estonia experienced the earliest economic recovery. Estonian GDP hit bottom in 1994, and staged a remarkably steady recovery since. Energy trade reorientation and movement toward world-market prices began early and continued in the post-1994 period. Energy efficiency has also been on the increase. Energy use per unit of GDP continued its downward trend, indicating that the economic recovery has been

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<sup>26</sup> Ibid.

based in the growth of less energy-intensive sectors. Indeed, the fastest-growing sector in the Estonian economy was services, and heavy industry suffered one of the worst declines. Energy consumption by industry hit its low in 1993, at 77% of 1992 industrial consumption and a mere 45% of 1991 industrial consumption. It has risen slowly since, to roughly 87% of 1992 levels by 1996, but most of the increase has been in newer and more efficient industries. How can we explain this rapid transformation? Estonia has managed to maintain a consistent stance in three key policy areas (foreign policy, macroeconomic policy, and energy policy), despite the economic hardships these policies have inspired.

### *Foreign policy*

Estonian post-independence foreign policy stands on three pillars: accession into the European Union; membership in the security structures of Europe, including NATO; and good neighborly relations, with Russia specifically. These goals have remained consistent across Estonian governments. It is the last pillar -- good neighborly relations with Russia -- which has been least vigorously pursued by all Estonian governments. Relations with Russia have been rocky. Despite Russia's acceptance of independence in 1991, the last Russian troops did not withdraw from Estonian soil until 1994. Even after this, economic relations with Russia remained politicized:

Economic relations with Russia are not purely economic relations, they are political, and very often the politics takes the upper hand. Relations between a superpower, the Soviet Union and Estonia, a small break-away republic cannot always develop in a very fast and

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<sup>27</sup> Interview with author, Leivi Sher, Advisor, United People's Party of Estonia Faction, Estonian Parliament, October 19, 1999.

friendly way. We are always interested in maintaining friendly relations with Russia, but the superpower Russia has its own ideas about its so-called "little brothers." It means that on the one hand, economic interests between our countries exist. But also they are very much influenced by the politics.<sup>28</sup>

Estonia also chose not to join the Commonwealth of Independent States, a Russian-led economic association established in after the fall of the Soviet Union. "This door was open, but Estonia and the other Baltic states refused."<sup>29</sup> There was quite widespread political consensus on this point in the Estonian government, and very little electoral pressure on the government to pursue CIS membership. This was in great part due to the fact that those sectors which would benefit most from the maintenance of a trade union with Russia, those who depended most on energy subsidies and Russian export markets such as heavy industry, were politically excluded:

Things were such that all of the larger industrial enterprises contained a workforce of mainly Russian origin. So Estonians as such were not so much engaged in industry. This is in some way a nationality question, because in all of those large enterprises, those thousands of workers were only Russians, immigrants... Rarely were there Estonian workers... There were so few Estonian workers, that there was not any pro-CIS political pressure on the government.<sup>30</sup>

Estonian governments have been more enthusiastic in support of the other two foreign policy goals. Estonia has been remarkably successful in its bid to join the European Union, and is now on the fast track for membership. Entire government agencies have been established to pursue membership, and many painful reforms have been enacted with an eye increasing prospects of European integration. Government

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<sup>28</sup> Interview with author, Andres Traat, Second Secretary, External Economic Policy Department, Ministry of Foreign Affairs, Tallinn, Estonia, October 20, 1999.

<sup>29</sup> Ibid.

<sup>30</sup> Ibid.

support for these agencies and reforms, despite the expense, was unwavering. Estonia also received membership in the World Trade Organization in 1999.

There was also some hope that EU membership might eventually take some of the pressure off of Estonia in terms of its relations with Russia:

Within the framework of the European Union, our policy would be the general policy of EU... So it would make our relations more universal. If Estonia were a member of the EU, it would mean that Estonian citizens would free to move about and it would also deconcentrate the pressure from Estonia. <sup>31</sup>

Accession would mean acceptance of European Union policies, including those on visas and immigration. This would effectively tie Estonia's hands, removing the responsibility of those policies unpopular with Russia from the shoulders of Estonia, placing them with the European Union.

Estonia, along with the other Baltic states, has been less successful in gaining NATO membership. Estonia has consistently pursued this goal, despite the fact that the third stated foreign policy goal, good relations with Russia, was at times at odds with Estonia's NATO aspirations. When a conflict arose, it was clear that establishing friendly relations with Russia was secondary. A representative of the Estonian Foreign Ministry describes the thinking behind these policies:

There is no doubt that this [Estonia's pursuit of NATO membership] has a negative impact on relations with Russia. But there are several theories about these borders between civilizations. We consider our civilization Western. But the border with the Eastern civilization runs between Estonia and Russia, between West and East. It means we have to accept all of those risks and hazards that come with being on the border of civilizations. But of course this is simply the way it is. At the present time it is negative, but during in the long run, Russia will have to understand that there is no other way. <sup>32</sup>

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31 Ibid.

32 Ibid.

While the Estonian government continued to pursue NATO membership, it understood that this membership might not be immediately forthcoming. Estonia is seeking membership in other security structures of Western Europe as well.

Estonian foreign policy has sought engagement and integration into the global, and particularly Western, markets, security structures, and international organizations, quite often at the expense of its relations with Moscow. The consistency of this policy across governments and the credibility that such consistency has afforded the Estonian government in the eyes of the international community, have encouraged the Western investment and aid which have underwritten Estonia's economic transformation.

#### *Economic policy*

Estonia has been equally consistent in its pursuit of pro-market, liberal macroeconomic policies, which has led to mass privatization and dramatic restructuring of the economy. Whereas industry was the largest sector of the Estonian economy in 1991, comprising 38% of the economy, it was surpassed by the less energy-intensive service sector which, by 1997, accounted for a massive 63% of the economy, up from 32% in 1991. New, less energy-intensive light industries have also begun to flourish. This restructuring had paid off: by 1997, Estonia's GDP was growing 9% per year.

The keystones of Estonia's liberal economic policies have been almost complete privatization, a balanced national budget, stable exchange rate, and a simple and transparent tax regime. The policies were adopted early in the transition process, and maintained thereafter. As was mentioned earlier, there was broad consensus on liberal

economic reforms across the governments. Such consistency in liberal macroeconomic policy helped Estonia attract the investment necessary for economic recovery and energy trade reorientation. In addition, Estonia also pursued a policy of seeking direct foreign investment, and quite successfully. It established the Estonian Investment Agency, under the direction of the Ministry of Economy, for the express purpose of attracting foreign direct investment. A representative of the EIA explains its mission: "We are a promotional organization, and what we want to sell is the investment climate we have here in Estonia."<sup>33</sup> The "selling points" of the Estonian investment environment are many, including near-complete privatization (80%), a stable currency, a budget required by law to be in balance, liberal trade, and low taxes.<sup>34</sup>

Estonia also streamlined its tax system, reducing corporate taxes and increasing the simplicity and transparency of the tax codes as much as possible in order to promote investment. A flat corporate tax of 18% was instituted. Incentives for reinvestment of profits were also to be introduced, making such reinvested revenue tax-free.<sup>35</sup> By 1999, the overall tax burden in Estonia as a percentage of GNP, including payroll taxes and individual income taxes, was 37%. Import duties were minimized, applying mainly to luxury goods and fuel. Export duties were all but eliminated.<sup>36</sup>

Labor costs, while they increased during the transition period, remained markedly lower than in Western Europe:

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<sup>33</sup> Interview with author, Alar Kaup, Energy Project Manager, Estonian Investment Agency, Estonian Investment and Trade Development Foundation, October 18, 1999, Tallinn, Estonia.

<sup>34</sup> Ibid.

<sup>35</sup> Interview with author, Arvi Karotam, Chairman, Estonian Investment Agency, Estonian Investment and Trade Development Foundation, October 18, 1999, Tallinn, Estonia.

We are promoting the fact that we have low labor costs, but it is still well-trained and well-educated labor. We are also promoting our education system. It is quite good. And our people are Western-minded. The cultural background is more or less European. Germany and Finland have had a very close relationship with us historically. The working culture is quite good.<sup>37</sup>

The Estonian government and Investment Agency tout the attractiveness of Estonian labor not only on the basis of lower wages, but also on its purported high quality, education and Western-orientation. The nature of Estonian culture is promoted as European in an argument that it may integrate seamlessly with the economies of Western and Northern Europe.

The economic policies put in place in Estonia in order to attract Western investment and trade have been highly successful in facilitating Estonia's rapid energy trade reorientation and economic transformation. These policies have not been without cost, however. The self-imposed constraints of low tax burdens and balanced state budgets have necessitated an enormous contraction in state spending. Wide-spread privatization has led to increases in efficiency, and with them massive lay-offs. Policies to facilitate Western investment and trade, along with a foreign policy which has ensured rocky relations with Russia, have undermined traditional import relationships and export markets, most notably with Russia. Nowhere were these hardships more keenly felt than in the heavily industrialized northeastern and Tallinn areas. "For industry, one of the biggest problems was probably the loss of the export market. We produced previously for the Russian market and those of other Soviet republics. And this market was in

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<sup>36</sup> Interview with author, Alar Kaup, Energy Project Manager, Estonian Investment Agency, Estonian Investment and Trade Development Foundation, October 18, 1999, Tallinn, Estonia.

<sup>37</sup> Ibid.

ruins.”<sup>38</sup> Heavy industry had been geared for production for Soviet markets. The dissolution of the Soviet Union led to a decline in Russian consumption overall, and a decline in imports from Estonia in particular. This is not simply a result of declining Russian consumption, however. It is also a result of the Russian government’s decision to stop importing many Estonian goods.<sup>39</sup>

First of all, energy-intensive and raw-material-intensive industries collapsed. In Soviet times, some or even most of them were connected with the Russian military complex. So now we that have no need of them, they have collapsed... Only small portions of these have managed to restructure for new production.<sup>40</sup>

These and other heavy industries were caught in a trade vise; they depended on raw-material imports, particularly fuels, from Russia (these industries were generally highly raw-material and fuel intensive, yet Estonia could produce few of these inputs domestically), and again dependent on Russian export markets for sale of final production. The Russian military no longer purchased from Estonian factories, driving many of these factories to close. Even if the inefficient non-military factories could have found new markets for their production, they needed access to inexpensive Russian inputs for their production processes to survive. Because state subsidies for these industries were not forthcoming, as trade relations with Russia collapsed, so did these industries and the economies of the northeastern regions.

Some reallocation of these resources began to take place, but on a limited scale and at a fraction of previous employment levels:

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<sup>38</sup> Interview with author, Villu Vares, Ph.D., Head of Energy Economy and Planning Laboratory, Estonian Energy Research Institute, October 21, 1999, Tallinn, Estonia.

<sup>39</sup> Russia continued to import many similar goods from other NIS, such as Belarus, despite its domestic economic difficulties.

I think we fully lost the Russian market, and by 1999 what manufacturing industries we have, with the exception perhaps of food processing, are oriented almost 100% to new production. Oil shale mining is the exception, but that is not exported. But we had a few very big military factories, but there is no demand for this production now. <sup>41</sup>

Why did not these populations resist these policies in the very earliest stages of the transition, which would soon displace them and derail their regional economies? Part of the explanation may be that they did not immediately understand that the policies would lead to industrial closure and unemployment:

The problem was that these people [industrial workers], they were not educated in market economy. They did not understand at this time how to find a market. Marketing is of course an absolutely new area for these people. They never thought about it because [during the Soviet time] it was not important. All production was requested in advance. They had no "department of marketing". The main task in Soviet times was how secure raw materials. That was a very big department in every factory. But no marketing. Because it was all planned state production. I think this was the main problem. <sup>42</sup>

In the beginning, the workers in these factories may not have realized that there would be no market for their goods. By the time they understood the effect liberalization would have on their livelihoods, the voting restrictions may have already been in place.

There is evidence that the rightist economic policies of the Estonian government would not have been sustained were all residents allowed to vote. A representative from the United People's Party of Estonia, a national party which is supported by and promoted the interests of Russophone residents, summarizes the problem:

The economic policy of the government is very, very right-wing. In the first period of our independence, we paid too much attention to quick economic development, and social problems were neglected. Because of this neglect, our social problems are now very

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<sup>40</sup> Interview with author, Anton Laur, Ph.D., Senior Researcher, Energy Group, Estonian Institute of Economics at Tallinn Technical University, October 18, 1999, Tallinn, Estonia.

<sup>41</sup> Interview with author, Villu Vares, Ph.D., Head of Energy Economy and Planning Laboratory, Estonian Energy Research Institute, October 21, 1999, Tallinn, Estonia.

<sup>42</sup> Ibid.

large. These problems are very dangerous because our social and nationality problems together pose a very great danger for the Estonian state. <sup>43</sup>

Mr. Sher refers specifically to the fact that the economically depressed, previously industrialized areas which have suffered as a result of the extreme right-wing policies of the Estonian government are also those populated by Russian-speakers. Inattention to these problems in the long run may prove dangerous to the Estonian system, he argues, even if not through the ballot box.

The problems of industry and energy production specifically in these areas are manifold. Soviet-era industrialization and mining had taken place with little regard for environmental impact, leaving a deeply polluted region with serious implications for public health. The unemployment which has resulted from the industrial decline has produced periodic bouts of social unrest. These issues were intertwined with nationality issues of an ethnic and linguistic minority which feels, justifiably, disenfranchised.

It is a very complicated area. First, there are environmental problems connected with the energy complex and other industries. There are Russian-speaking people are concentrated in Tallinn and in this area. Because of official policy in Soviet times, these industries were based on the labor coming in from other parts of Soviet Union. Half of the electricity produced was used for export to the northeastern region of the Soviet Union. <sup>44</sup>

The main Soviet-era industry still standing in this region are the electric power plants at Narva. As mentioned above, these plants were designed to be staffed by Russian immigrants, and to export half of their production to Russia. These plants are fueled by Estonia's sole substantial indigenous energy resource, oil shale. The oil shale mines are

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<sup>43</sup> Interview with author, Leivi Sher, Advisor, United People's Party of Estonia Faction, Estonian Parliament, October 19, 1999.

<sup>44</sup> Interview with author, Anton Laur, Ph.D., Senior Researcher, Energy Group, Estonian Institute of Economics at Tallinn Technical University, October 18, 1999, Tallinn, Estonia.

also mainly located in this region, and mainly staffed by Russian-speakers. With the loss of the Russian export market, as well as a decrease in Estonian consumption, the demand for Narva's electricity has fallen to a fraction of previous levels. Operating the plants so far below capacity has only exacerbated the inefficiency of these already outdated generators and mines.

Some of our factories in Kosloyarov stopped working. We now have problems at the Narva power stations. Because we do not need as much electricity as they produce, 600 workers must be fired. This is a very great problem for us. We are afraid that power-station privatization will result in more than 40% unemployment in the region. It is a very difficult problem for us.<sup>45</sup>

Estonian policy in this matter was consistent with its overall economic strategy: privatize, marketize, and attract Western investment. Estonia invited the US company NRG Energy to purchase and modernize the plants, increasing efficiency and profitability with the introduction of contemporary technology. However, after the overhaul is complete, this may eventually mean even greater levels of unemployment in the region, as the director of NRG Energy's Estonian operations states. While employment over the next 5 years, during the investment and reconstruction phase, may remain relatively stable, "Direct jobs as workers in the power plant will probably be reduced."<sup>46</sup>

While the Estonian government was very interested in attracting foreign direct investment for technological purposes, particularly in Narva,<sup>47</sup> it was also aware of the pending implication for so-called "social problems".

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<sup>45</sup> Interview with author, Leivi Sher, Advisor, United People's Party of Estonia Faction, Estonian Parliament, October 19, 1999.

<sup>46</sup> Interview with author, Hillar Lauri, Director, Estonian Operations, NRG Energy, October 18, 1999, Tallinn, Estonia.

<sup>47</sup> Interview with author, Villu Vares, Ph.D., Head of Energy Economy and Planning Laboratory, Estonian Energy Research Institute, October 21, 1999, Tallinn, Estonia.

There is a “social” working group [with the government and NRG Energy]. The government has realized that this situation could explode if we don’t deal with the social issue. So we are negotiating about levels of employment, salaries to be paid. We are paying millions of dollars extra because of these social problems, so that people are not just paid the legal minimum... because that could create problems. <sup>48</sup>

Thus foreign direct investment becomes a means of social support, and seeking it a strategy for ameliorating future problems.

### *Energy policy*

Estonia gained energy independence from Russia earliest and most completely of all the cases. It did so through a combination of pragmatic strategies geared toward reducing vulnerability to Russian supply cuts given the practical constraints in each energy sector. Estonia opened up its oil market even before independence, and freed prices and controls, and built new import facilities as soon as possible after independence. This has led to substantial and rapid supply reorientation toward Western Europe. In sectors where the costs of infrastructure for supply reorientation were prohibitive in the short-term, Estonia promoted large-scale strategic investment by Western companies to balance the concerns, and control, of Russian suppliers. This has been the near-term strategy in the gas sector. Where the Russian presence was necessary in the near term, such as in the transportation and gas through-put sectors, Estonia sought to increase Russian interests in delivery by privatizing, at least in part, to ethnic Russians and moving to cash payments at world-market prices. Lastly, in order both to maximize development of indigenous resources (thus decreasing reliance on imports altogether) and to help

ensure the security of the Russophone northeastern regions. Estonia invited in private strategic American investors to restructure and run its electricity-generating power plants and oil shale mines.

Prior to independence, Estonia had been thoroughly integrated into the Soviet energy system: it imported all of its natural gas, fuel oil and gasoline from Russia, and exported half of its electricity production – the only substantial domestic energy resource – back to Russia, making the sustainability of this industry dependent upon access to the Russian market. It broke this dependence through a combination of policies including encouraging an overall decline in energy consumption: allowing large energy-intensive industrial consumers to falter and even to fail; early investment in infrastructure (most notably, ports) to facilitate imports from the West, along with a political willingness to pay higher Western prices; and privatization of oil, gas and electric industries including the support of strategic investment through East-West partnership to encourage security of supply.

Russia placed a fuel embargo on Estonia following the referendum on independence in 1990. This blockade coincided with the first of several harsh winters, causing widespread hardship in Estonia. The blockade ultimately proved ineffective, however. “The blockade did not last long because Estonians very quickly reorganized their supply of fuel from the West. And so Russia saw that there was no point in

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<sup>48</sup> Interview with author, Hillar Lauri, Director, Estonian Operations, NRG Energy, October 18, 1999, Tallinn, Estonia.

continuing the blockade.”<sup>49</sup> Estonia had established a relationship with the Finnish Neste<sup>50</sup> corporation during the Gorbachev years, importing small amounts of gasoline from the West even prior to the fall of the Soviet Union. This early connection helped to ease the transition.

We have partner [Scandinavian] companies, like Neste and other companies here in Estonia, because we are near and there are past connections there. And there was a preparation period, at the beginning of Gorbachev time, it was not even the transition yet, when we made the connection and prepared for the process of transition.<sup>51</sup>

One of the most remarkable aspects of Estonia’s energy trading patterns is how early Estonia began its energy import diversification, and how thoroughly it has progressed. Of the three most important energy imports (by value), petroleum spirit for motor vehicles, diesel oil, and natural gas, by 1999, non-Russian suppliers posed serious competition in two. Finland was the primary source of petroleum spirit, and had been for some time. Finland was also an alternative supplier in the diesel oil market, in which it was even primary supplier by 1997. While detailed statistics are not readily available, according to an interviews with a Neste Oil Company and Estonian Ministry of Economics representatives,<sup>52</sup> large-scale oil exports to Estonia from Finland began virtually immediately after the blockade was imposed. Also quite striking is the fact that

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<sup>49</sup> Interview with author, Andres Traat, Second Secretary, External Economic Policy Department, Ministry of Foreign Affairs, Tallinn, Estonia, October 20, 1999.

<sup>50</sup> Interview with author, Arvi Karotam, Chairman, Estonian Investment Agency, Estonian Investment and Trade Development Foundation, October 18, 1999, Tallinn, Estonia.

<sup>51</sup> Interviews with author, Anton Laur, Ph.D. and Koidu Tenno, Ph.D., Senior Researchers, Energy Group, Estonian Institute of Economics at Tallinn Technical University, October 18 and 21, 1999, Tallinn, Estonia.

<sup>52</sup> Interview with author: Tapio Jarvinen, Direct Sales Europe Director, Neste Oil Company, 10/13/99, Vilnius, Lithuania.

this reorientation took place while Russian prices were significantly lower than those of Finland.

Yet trade reorientation posed serious financial difficulties. Large-scale energy trade reorientation began in 1992:

At first, in 1992, it was very difficult because the price from other countries, even in Finland, was very high. For this reason it was difficult to buy from Finland immediately. And of course there were no facilities in our port for tankers or to import fuel oil from other countries and by sea. It had traditionally been by railway from Russia; it was easier. But it [reorientation] happened very quickly. We now buy it from Finland and, of course, we buy from Russia, too. All of these prices are now all based on Rotterdam [world market] price.<sup>53</sup>

Estonia increased fuel imports from Finland at world-market prices, and began immediate investment in port facilities, despite the economic hardship the country was experiencing. Investment in oil import facilities in Estonia's ports began "just the first day when we suddenly became again independent. It is evident from the state of our ports compared with ten years ago that tremendous investment was put in there."<sup>54</sup> Russian energy prices to Estonia had begun increasing slightly in the late 1980s. After the blockade, and Estonia's refusal to capitulate to Russia's demands, Russian prices began to rise dramatically. Prices rose "from about practically zero up to about perhaps 70% of Western Europe prices, in one and a half, two years."<sup>55</sup>

Estonia was very active in building new means by which to diversify its energy suppliers. It began upgrading oil and gas terminals and facilities to increase imports from

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<sup>53</sup> Interview with author, Ell-Mari Koppel, Head of Energy Department, Ministry of Economic Affairs, Republic of Estonia, October 21, 1999, Tallinn, Estonia.

<sup>54</sup> Interview with author, Arvi Karotam, Chairman, Estonian Investment Agency, Estonian Investment and Trade Development Foundation, October 18, 1999, Tallinn, Estonia.

<sup>55</sup> Interview with author, Villu Vares, Ph.D., Head of Energy Economy and Planning Laboratory, Estonian Energy Research Institute, October 21, 1999, Tallinn, Estonia

the West fairly early after independence. While Estonia continued to import energy from Russia, it did so at near-world-market prices. It also began serious diversification; Finland soon became Estonia's primary supplier of certain energy inputs. The Estonian retail gasoline market by 1999 was dominated by Scandinavian companies such as Neste and Statoil. Furthermore, a Canadian company was exploring the possibility of refining Estonian oil shale into fuel oils.<sup>56</sup> This would reduce Estonia's vulnerability even further.

Estonia pursued a policy of trade reorientation in its broader economic relations as well. Whereas Russia was Estonia's largest trading partner in 1992, by 1997, it had been supplanted by Finland, Sweden and Germany. Why did Estonia make this transition when other NIS did not? A senior energy researcher in Estonia places most of the credit with the policies of the right-wing government:

One [way in which Estonia differed from many NIS] was that the first, main parties who were in the parliament were very right-wing parties...They supported very liberal market policies from the very beginning. Of course, for about 2 years, it was terrible for people, cold apartments and so on. But after that, our people managed a little. And maybe such a shock was successful. I did not support this policy 100% this time, but now it seems that it was transformation. Lithuania [which has lagged behind] was much more careful. Almost the same decisions were made in Latvia as in Estonia, but a little bit later.<sup>57</sup>

Russia made subsequent threats of fuel blockades, principally in connection with Estonia's treatment of its Russian-speaking minority.<sup>58</sup> Estonia undermined the effectiveness of future Russian fuel and gas blockades through two strategies: diversification and co-optation. The rapidity of Estonia's oil trade reorientation

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<sup>56</sup> The technical feasibility of this venture is still in question.

<sup>57</sup> Interview with author, Villu Vares, Ph.D., Head of Energy Economy and Planning Laboratory, Estonian Energy Research Institute, October 21, 1999, Tallinn, Estonia.

<sup>58</sup> Interviews with author, Anton Laur, Ph.D. and Koidu Tenno, Ph.D., Senior Researchers, Energy Group, Estonian Institute of Economics at Tallinn Technical University, October 18 and 21, 1999, Tallinn, Estonia.

undermined the effectiveness of Russia's actual and threatened fuel blockades. In terms of natural gas, it is hoped that gas storage facilities in Latvia may prove a further cushion against Russian-imposed shortages.

[Russian fuel blockades are] not very effective any more. In Latvia, we have gas reserves for one year for Estonia. It means that we will always have these gas reserves in Latvia. We have our reserve, and there is no point to cutting now the supplies, because, now we have other ways to secure supplies. They are more expensive, but they exist.<sup>59</sup>

A key to early energy-trade reorientation for this cash-strapped state was conservation, not a massive drop in energy consumption. Estonia attempted to increase reliance on domestic energy resources in order to minimize the necessity of imports. Imports of fuels after independence, between 1990 and 1996, fell by over 40%. Yet Estonia's energy resources were extremely limited, consisting of wood, peat and oil shale.<sup>60</sup> Maximizing energy self-sufficiency given such limited resources necessitated increased efficiency. To the right-wing government, this meant marketization, privatization, and price liberalization.<sup>61</sup> Domestic energy prices were liberalized early and dramatically.

All our prices now are free. We do not regulate the prices now on fuel. We have an antimonopoly law in the energy sector, so that if some energy or fuel company dominated in the market, over 40%, then they would have to present the price to our energy-market inspectorate for approval. But no company currently has 40% in this market, so it is a totally free market price.<sup>62</sup>

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<sup>59</sup> Interview with author, Andres Traat, Second Secretary, External Economic Policy Department, Ministry of Foreign Affairs, Tallinn, Estonia, October 20, 1999.

<sup>60</sup> Interview with author, Alar Kaup, Energy Project Manager, Estonian Investment Agency, Estonian Investment and Trade Development Foundation, October 18, 1999, Tallinn, Estonia.

<sup>61</sup> All of the large energy enterprises have been privatized, or are in the process of being privatized, including energy distribution networks.

<sup>62</sup> Interview with author, Ell-Mari Koppel, Head of Energy Department, Ministry of Economic Affairs, 10/21/99, Tallinn, Estonia.

These prices have been free since the beginning of the market period. The state does not set energy or fuel prices. Instead, the state maintains an anti-monopoly commission:

We have a free market for selling fuel prices with no subsidies for fuel or electricity. To some extent, there is subsidizing within the electricity-producing system: industrial consumers are subsidizing of households. This also has decreased, step by step. Now we have adopted an energy law, which established the energy market inspectorate. Before it there was a so-called price commission, which was specially formed by the ministry of economics, and consisted of experts which analyzed proposals of energy firms, oil shale mining firms and electricity-producing firms. So mining of oils shale price and electricity price were under state control. But the fuel prices, they were free from the beginning of the transition period. It was a "shock" period. But now it is over.<sup>63</sup>

While the state did not provide direct subsidies of energy prices, it did demand that industry do so. "We have some small cross-subsidization between industry and householders. If we raise the electricity price, the rise is smaller for householders than for industry -- if the price is small for householders, then the price for industry is higher."<sup>64</sup> Such cross-subsidization cushions households from high energy prices and penalizes energy-intensive industries. This strategy has been fairly successful. While domestic energy production fell after independence, it subsequently recovered showing an increase across the board by 1996. By 1999, 60-65% of Estonia's primary energy needs were met by indigenous oil shale.<sup>65</sup>

A key to Estonia's strategy of reducing consumption, increasing domestic energy efficiency, reducing imports and increasing security of supply has been energy sector

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<sup>63</sup> Interviews with author, Anton Laur, Ph.D. and Koidu Tenno, Ph.D., Senior Researchers, Energy Group, Estonian Institute of Economics at Tallinn Technical University, October 18 and 21, 1999, Tallinn, Estonia.

<sup>64</sup> Interview with author, Ell-Mari Koppel, Head of Energy Department, Ministry of Economic Affairs, 10/21/99, Tallinn, Estonia.

<sup>65</sup> Ibid.

privatization and securing strategic investment. Privatization of oil-related concerns began early. Since Estonia produces no oil itself, these consisted of gas stations, transportation and import companies (railway lines) and some port facilities. Western oil companies in particular engaged in this process, coming to dominate the gasoline market in Estonia. Neste of Finland and Statoil of Norway began buying and building gas stations, importing the gasoline from their own refineries in the West. Texaco and Shell soon followed suit.<sup>66</sup> This quickly gave Estonia an alternative supplier for gasoline and other oil products, including heavy fuel oils, reorienting imports of those goods westward.

Reorientation of imports in the natural gas sector proved more problematic, however. Building new infrastructure for the import of natural gas from the West would have been considerably more difficult and expensive than for importing oil, given the volatility of the substance. Of all energy imports, it is only in the natural gas market that Russia retains its monopoly. According to the Estonian Ministry of Economy,<sup>67</sup> future energy plans include and increasing reliance on natural gas in heating and perhaps also in energy generation. Russia is now, and has been, the only supplier of natural gas to Estonia.

Estonia has chosen to address the problems this poses for security of supply through strategic joint ownership agreements. Estonia sold a portion of its domestic natural gas distribution company to Gazprom (which government representatives<sup>68</sup> argue

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<sup>66</sup> Interview with author, Alar Kaup, Energy Project Manager, Estonian Investment Agency, Estonian Investment and Trade Development Foundation, October 18, 1999, Tallinn, Estonia.

<sup>67</sup> Interview with author, Ell-Mari Koppel, Head of Energy Department, Ministry of Economic Affairs, 10/21/99, Tallinn, Estonia.

<sup>68</sup> Interview with author, Sten Schwede, Ministry of Foreign Affairs, External Economic Policy Department, 10/18/99, Tallinn, Estonia.

gives Gazprom a financial interest in reliability of supply and has helped avoid Russian-imposed natural gas shortages) and part to Ruhrgas, a German company, which provides capital, reliability of supply, and a Western partner.<sup>69</sup> The German natural gas company Ruhrgas was sold the largest portion, giving it the most control over the company. A large portion was also sold to the Russian company Gazprom, which continues to supply the natural gas itself. A share was retained by the Estonian government, and small portion later sold to the Finnish energy company, Neste. This arrangement was intended to increase the security of supply. “They [Gazprom] have a big financial interest to keep this business. It was strategically the right decision, from Estonian side, to have a state portion of the gas company, and Ruhrgas.”<sup>70</sup>

According to Estonian experts on the energy industry and market, this strategy has proven remarkably successful:

I think this combination, a very powerful gas company in Europe, AND a big Russian company, the producer of the gas, gives us quite good security of supply. And probably it was the main reason in the beginning in the '90s that we had no problems with gas supply. Other Baltic states had such problems, and the decision of our gas company was good. They sold 20% of shares to Gazprom in the beginning. That [the Estonian gas company] is a very successful company just now.<sup>71</sup>

In fact, the strategy has been so successful that Latvia soon emulated Estonia's policy, inviting Ruhrgas and Gazprom to take shares in its natural gas company's privatization.<sup>72</sup>

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<sup>69</sup> The “Baltic Ring” project is a possibility for expanding into Scandinavian sources. This project is still highly ephemeral, as funding has not been found. It may, however, be taken as an indication of Estonia's interest in source diversification and Westernization.

<sup>70</sup> Interview with author, Arvi Karotam, Chairman, Estonian Investment Agency, Estonian Investment and Trade Development Foundation, October 18, 1999, Tallinn, Estonia.

<sup>71</sup> Interview with author, Villu Vares, Ph.D., Head of Energy Economy and Planning Laboratory, Estonian Energy Research Institute, October 21, 1999, Tallinn, Estonia.

<sup>72</sup> Ibid.

Estonia also privatized the through-put, or oil-transit, companies, which had grown substantially since independence, and had sold them principally to Russian-speaking residents. These policies may help to define a new set of incentives for Russian suppliers.

The Estonian fuel companies have kept a relationship with Russia, and they have a very good relationship with the Russian companies. The Russians are very interested in selling fuel abroad, because from Estonia they receive payment, but from inside the Russian country they often do not. In part because of the more reliable payments, they are interested in working with Estonian companies.<sup>73</sup>

Estonian officials speculate that Russian-speaking transit companies may be able to maintain better relationships with Russian suppliers, and may make blockades more problematic for Russia domestically, as it is the Russians living abroad who would suffer from stoppages. On-time cash payments and world market prices make Estonia a valued customer for Russian companies accustomed to selling on the domestic Russian market. Lastly, the predominance of Western suppliers in Estonia makes threats of blockade ineffectual. Estonia may eventually succeed in transforming oil trade with Russia from a political tool into a normalized economic exchange.

The last large privatization in the Estonian energy sector was that of its electric plants in Narva. Estonia was self-sufficient in electricity production, and possessed the capacity for substantial exports. However, the plants which generated this electricity stood in dismal disrepair, were inefficient and uncompetitive by Western standards, and were an environmental disaster. It is not only to increase efficient use of domestic

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<sup>73</sup> Interview with author, Ell-Mari Koppel, Head of Energy Department, Ministry of Economic Affairs, 10/21/99, Tallinn, Estonia.

resources that the Estonian government decided to privatize the Narva plants, but also for preparation for entry into the European Union.

[Oil shale] is one of the dirtier fuels. But it can be burned more cleanly. One reason to do this [privatize to a Western investor] is obviously the accession to the EU and EU environmental guidelines. The project is designed around that schedule. So that's really what's driving it.<sup>74</sup>

European union membership would also entail competition in the domestic electricity market, making efficiency at the Narva plants essential.

Estonia signed deal with NRG Energy, an American company, to sell 51% of electricity-generating company and 49% of domestic oil shale resources in exchange for investment and modernization of these resources. These resources were to be found in the Russian-populated Narva and northeast counties. The generation stations were only miles from the contested Russian border. According to the Director of NRG Estonia,<sup>75</sup> this was a strategic decision on Estonia's part. Representatives<sup>76</sup> from the foreign ministry acknowledge the strategic importance of an American investor in this project, which the Estonian government expressly sought. From the point of view of the US company NRG Energy, there were two reasons the Estonian government sought a US investor: the need to attract large-scale foreign direct investment in the plants, and the need for a specifically American presence on Estonia's Russian-populated borderland:

I (can) guess the reasons why the government has made up its mind finally that they need a strategic investor: one is that the plants are very old. The first boiler came into

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<sup>74</sup> Interview with author, Hillar Lauri, Director, Estonian Operations, NRG Energy, October 18, 1999, Tallinn, Estonia.

<sup>75</sup> Ibid.

<sup>76</sup> Interviews with author, Sten Schwede and Andres Traat, Ministry of Foreign Affairs, Tallinn, Estonia.

operation in 1959 and place is crumbling. They realized that if they don't do something soon like obtain large-scale investment, the place was going to fall apart.<sup>77</sup>

The director of NRG – Estonia describes the Estonian government's second goal, and its actions toward NRG Energy:

The Prime Minister went to the US at the end of 1995 to find a US company to put an American plant near the Russian border. The first visit of NRG to Estonia was December of '95. That was a clear part of the thinking. ... Major investors into Estonia have been by far from Finland and Sweden, and there was a need for some balance... [The Estonian government wanted to] try and get a large US investment here. It's called the "McDonalds effect". On your border, you put up all these McDonalds so that if they attack, they have to take over McDonalds. These power plants, close to the border... I'm hardly an objective observer, but I think it makes sense, because the most tension-filled region is NE Estonia, and if anything is going to blow, that is where it will be. And so wouldn't you want a large US investment there?<sup>78</sup>

The director of NRG – Estonia perceived the Estonian government as "a right-leaning government, in the sense of pro-investment, engaging, the outside world... (they) want more US investment in this country,"<sup>79</sup> particularly in the earliest years of the transition. While NRG was not given specific subsidies or targeted tax breaks for investing in Estonia, it was the only negotiating partner in the privatization. "In one sentence, we are the exclusive negotiating partner. This isn't tenured."<sup>80</sup> The offer was not open to other buyers. Rather, NRG Energy was sought out by the Estonian government. Levels of investment by NRG and help by the Estonian government are a matter of negotiation between the two entities.

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<sup>77</sup> Interview with author, Hillar Lauri, Director, Estonian Operations, NRG Energy, October 18, 1999, Tallinn, Estonia.

<sup>78</sup> Ibid.

<sup>79</sup> Ibid.

<sup>80</sup> Ibid.

*The trajectory of Estonian energy policy*

Estonia sought to achieve energy security, and succeeded to a great extent. There are limits to the energy autarky that a resource-poor country may achieve, however. While Estonia's oil shale may be used to produce electricity, this resource will eventually become depleted. And electricity is not enough: the infrastructure of Estonia is geared toward the use of natural gas and oil products in heating, transportation and many industrial applications. A Canadian company, Suncor, has been invited to research the possibility of processing Estonian oil shale into fuel oil and gasoline. The environmental, economic and technical feasibility of such an undertaking remains in serious question, however.<sup>81</sup> It is likely that Estonia will remain dependent on imports for its oil and natural gas needs. It has chosen to address this dependence through diversifying its suppliers and strategic "balancing" investments, thus reducing its vulnerability. By 1999, Estonia was paying world market prices for all oil imports, and it was paying them on time and in convertible currency. It had privatized the distribution networks.

The future of Estonian energy trade may also include expanded exports of electricity. Modernized generation and oil-shale mining in Narva may increase further Estonia's surplus capacity for export. The question will be, export to whom? Estonia's electricity infrastructure remains integrated physically with that of Russia.

In the [electricity] business, it is not very easy to become independent, because of the integration within a network. A lot depends on in which network; in the Russian network, or in Scandinavian network. Today it's natural [for Estonia] to be in Scandinavian network, and I think we will be. The question is, in terms of integration with Western Europe, could we get new investments in our plants to use oil shale

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<sup>81</sup> Ibid.

efficiently, and produce from this cheaper than others so we can sell it and use it ourselves? <sup>82</sup>

This poses problems not only technically (because of the frequency fluctuations leaking from across the Russian border), but also economically. Russia had been Estonia's main electricity export market, but consumption in Russia has declined. There are also problems of payment:

Russia has problems because their economy has declined. They also have problems making payments. We have deals to buy oil shale from Russia, and in exchange we sell electricity to Russia. But the export price has declined and we have no real desire to import more oil shale. <sup>83</sup>

Estonia's other current export market for electricity, Latvia, is, like Russia, an unreliable customer, but for different reasons:

Latvia has quite a substantial hydroresource, the river range that flows into the capital, Riga. Their imports depend on how much rain they get. In a very rainy year, they do not import much. In a dry year, they buy more. So it is not very stable. Last year, 1998, was bad in this sense, it was a rainy year in Latvia, and Russia had problems with payment. So the exports stopped. What little export there was, stopped. <sup>84</sup>

Whereas fully 50% of the electricity production in Soviet times was exported, by 1999 it was as low as 4%. The power stations which were built to supply the entire northwestern region of the Soviet Union are too large for Estonia to operate efficiently only for the domestic market.<sup>85</sup> The Estonian government is pursuing plans to integrate

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<sup>82</sup> Interview with author, Arvi Karotam, Chairman, Estonian Investment Agency, Estonian Investment and Trade Development Foundation, October 18, 1999, Tallinn, Estonia.

<sup>83</sup> Interviews with author, Anton Laur, Ph.D. and Koidu Tenno, Ph.D., Senior Researchers, Energy Group, Estonian Institute of Economics at Tallinn Technical University, October 18 and 21, 1999, Tallinn, Estonia.

<sup>84</sup> Interviews with author, Anton Laur, Ph.D. and Koidu Tenno, Ph.D., Senior Researchers, Energy Group, Estonian Institute of Economics at Tallinn Technical University, October 18 and 21, 1999, Tallinn, Estonia.

<sup>85</sup> Interview with author, Ell-Mari Koppel, Head of Energy Department, Ministry of Economic Affairs, 10/21/99, Tallinn, Estonia.

into Western markets instead. Such a project would necessitate not only great investment, but also an increase in efficiency of production:

This is the main problem in this area. We have to be more efficient, because if we access to EU, we have to open our markets and then our power stations will be on the market where all things depend on the price. And if they are not efficient, consumers will be able to buy from others. And of course for this market, we need an infrastructural connection between Central Europe and maybe Finland, which would require investment. We want to create a Baltic market and to be ready for this.<sup>86</sup>

Estonia along with other states in the North of Europe, are engaged in negotiations for the so-called Baltic Ring project, which would build an infrastructure integrating electricity and natural gas markets around the rim of the Baltic Sea. Estonia is in enthusiastic supporter of this:

We need another sources for security of supply, to be connected with Finland or Lithuania or other European partners. Same as with electricity, we have to be connected to the Nordic countries, and maybe the Central European, in gas and electric. Then it would be possible to create this so-called Baltic Ring.<sup>87</sup>

The electric portion of this project would be relatively less costly, and the Estonian government is optimistic that a Finland-to-Tallinn cable may be realized soon. The natural gas portion of the Baltic Ring project, building a ring of pipelines between the states, would be substantially more costly. Investors have yet to be found for this undertaking. For the moment, going ahead with the electric but not the gas portion may meet Estonia's needs, as the deal between Ruhrgas and Gazprom has helped to prevent massive shortages, and natural gas is a relatively small portion of primary energy consumption in Estonia:

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86 Ibid.

87 Ibid.

Natural gas is used for 11% of primary energy consumption. We use fuel oil and natural gas in our boiler houses, for heating. And gas is used for cooking, too. We hope that this percentage will be higher this year, but of course we do not want to shut down our (oil shale) mines [which compete with natural gas]. We will continue to use our oil shale to produce electricity.<sup>88</sup>

The challenge for Estonia comes from its plans to increase natural gas consumption. Estonia's oil shale deposits will eventually become depleted, and a new source of energy must be found. Secondly, oil shale, even when used efficiently, is a dirty fuel, and Estonia is under pressure from the EU to minimize the ecological impact of its electric plants. The moderate government forecasts are for a doubling in the share of natural gas consumption in the next 10-15 years.<sup>89</sup> Such a change would not be without its problems for the Estonian trade balance:

We have an environmental problem with this oil shale. We also have the social and region problems with this oil shale. So it is not possible to just move to natural gas. So we have to produce our electricity based on our oil shale, but hopefully with the use of cleaner technology. Of course, if we deplete this resource of oil shale, and buy all fuels and gas abroad, and use only this to produce electricity and heat, it would affect our trade balance, too, because we have to import.<sup>90</sup>

Additionally, the oil-shale mining and oil-shale-based electricity production are located in Russian-speaking regions, making their closure especially difficult on those populations.

In a reasonable way, and to take into account social and environmental problems, we have to find some central way... to create more jobs in this county because the main enterprises and the electricity producers and the oil shale producers. There is very little large industry anymore. We have to create industry and provide jobs to the people... Yes, and of course, there are mainly Russian-speaking people there, and it is very difficult for them to move to some other part of the country. They do not know other jobs. They have been

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<sup>88</sup> Ibid.

<sup>89</sup> Interview with author. Villu Vares, Ph.D., Head of Energy Economy and Planning Laboratory, Estonian Energy Research Institute, October 21, 1999, Tallinn, Estonia.

<sup>90</sup> Interview with author, Ell-Mari Koppel, Head of Energy Department, Ministry of Economic Affairs, 10/21/99, Tallinn, Estonia.

miners and workers in these power stations and they are not young, and so it is very difficult to move to other place in Estonia. It is not an easy task.<sup>91</sup>

Ultimately, however, Estonian policy is likely to remain consistent with its emphasis on security, particularly *vis a vis* Russia, marketization and internationalization, especially in the sphere of energy:

It is mostly a security problem. We have some large projects, which are very expensive, and it is not so easy to implement such projects. We have the Baltic Ring project, and also the Gas Ring project. For Estonia, first it is security supply problem. But it is connected, economics and politics. It is also preparing the larger free market. It's connected with restructuring our energy sector, which takes a very long time. Maybe on the one hand, it's not good it is going very slowly, on the other hand it maybe is not bad. It is a very big and very hard sector, requiring very big investments. We must be careful, it is very easy to destroy it. It is very easy to destroy it, and it is very, very hard to build.<sup>92</sup>

## **V. Summary of the Secondary Case: Latvia**

As in Estonia, Latvia's Russophones were generally concentrated in heavy industry. However, this sectoral concentration was slightly weaker, and geographical concentration much weaker, than in Estonia, making political exclusion of Russophones a less perfect insulator from the demands of heavy industry. The political disenfranchisement of this ethnic minority – even larger in Latvia than in Estonia – was even more complete in Latvia: Russophones were not allowed to vote even in local elections. This provided some political insulation to government, helping to maintain a series of right-wing reformist coalitions: the right-wing reformist coalitions of 1990-95, the moderated reformist coalitions of 1995-1997, and the return to the far right after 1997.

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<sup>91</sup> Ibid.

This constituted a slightly wider range of coalitions than those which ruled Estonia. However, there was broad agreement across coalitions on macroeconomic and energy issues.

### *History and nation*

Latvia sits between Estonia and Lithuania on the eastern coast of the Baltic Sea. Its 25,000-square-miles territory also borders Russia and Belarus to the east. The Latvian language is, like Lithuanian, a member of a subfamily of languages that use the Latin alphabet and are related to the Slavic group. The largest religious denomination in Latvia is Lutheran, followed by Roman Catholic and Russian Orthodox. Latvia's political history is quite similar to that of Estonia. It was ruled by the Livonian Teutonic Knights beginning in the thirteenth century, by Poland in the sixteenth, Sweden in the seventeenth, and by Russia in the eighteenth. It came under Bolshevik power in 1917, was occupied by the German army in 1918, and was recognized as an independent state in 1920. A democratic regime was briefly established, but fell to the military dictatorship of Prime Minister Ulmanis in 1934. Latvia was "incorporated" into the Soviet Union in 1940, ending its period of independence.

As in Estonia, exclusionary language laws played an important role in Latvian politics. Prior to World War II, 77% of residents of Latvia belonged to the titular majority. In stark contrast, by 1991, only slightly more than 50% of residents of Latvia were ethnic Latvian. Subsequent migration (Russians returning to Russia, and Baltic

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<sup>92</sup> Interviews with author, Anton Laur, Ph.D. and Koidu Tenno, Ph.D., Senior Researchers, Energy Group, Estonian Institute of Economics at Tallinn Technical University, October 18 and 21, 1999, Tallinn,

peoples returning from exile abroad) only slightly altered this balance. In Latvia, the 2.4-million person population was only 56% ethnic Latvian, 30% Russian, 4% Byelorussian, and 3% each Ukrainian and Pole.<sup>93</sup> While these language laws were initiated early in the independence era, strong support remained across coalitions. As late as February 1998, the parliament rejected legislation that would grant automatic citizenship to children born to non-Latvians. The ruling Fatherland and Freedom Alliance and Latvian National Conservative Party insisted that all members of the government agree that citizenship laws could not be changed without unanimous approval of coalition members.

The Latvian government argued that Latvia was not a “newly” independent state, but rather the legitimate successor to the independent Latvia born after WWI and occupied by Soviet forces after 1940. To them, 1991 marked the end of this occupation and the reassertion of independence, not the creation of a new state. After this reassertion of independence, the legislature ruled that only residents descended from pre-1940 Latvian citizens would automatically be granted citizenship. As a result, only about 200,000 of the more than 900,000 Russian-speakers living in Latvia in 1991 were eligible for automatic citizenship. Naturalization procedures were later established, resting on demanding language requirements. A strong command of both written and oral Latvian became necessary for citizenship. This was problematic for many Russophones, as while most Latvians had learned Russian, few Russians had been required to learn Latvian under the Soviet regime. *De facto* yearly quotas on naturalization were implemented. The rights of non-citizen residents were quite limited: resident non-citizens could vote in

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Estonia.

neither local nor national elections, nor were they allowed to hold elected office. The requirements for residency permits themselves were also quite onerous.

The Russian population of Latvia was to be found mainly in industrial centers and urban areas, while the rural areas were mainly populated by the titular majority. For example, in Riga, the capital of Latvia, the majority of the population was actually Russian-speaking. The Latgale region of Latvia had a large proportion of Russian-speaking residents. While the geographical distribution of Russophones was somewhat less stark in Latvia than in Estonia, there was still great sectoral concentration. As in Estonia, in Latvia, ethnic Russians were brought to Latvia as skilled and unskilled labor in the growing industrial complex.<sup>94</sup> The largest portion of Russians and other Russophones in Latvia remained workers in heavy industry.<sup>95</sup> Long after the end of the Soviet Union, economic sectors and individual businesses in Latvia remained largely ethnically segregated. In addition to industry, Russophones also dominated the transit and banking (though Latvians were making inroads into this sector) industries, while ethnic Latvians dominated sectors such as agriculture, alcohol production, and wood-working.<sup>96</sup>

As in Estonia, Russophone residents in Latvia tended to favor more left-wing economic and social policies and closer ties with Moscow. Because Russophone Latvian residents were not allowed to vote even in local elections (unlike in Estonia), we cannot

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<sup>93</sup> CIA *World Factbook*, 1999.

<sup>94</sup> Edward Allworth, ed. *Nationality Group Survival in Multi-Ethnic States: Shifting Support Patterns in the Soviet Baltic Regions* (New York: Praeger Publishers, 1977), p. 92.

<sup>95</sup> Marja Nissinen *Latvia's Transition to a Market Economy* (New York: St. Martin's Press, 1999), p. 219.

<sup>96</sup> *Ibid.*, p. 242.

contrast national with local election patterns to divine their probable national voting positions. Instead, survey data and the results of Latvian residents' participation in Russian elections will be used.

In the early days of the independence movement, some Russophones supported the effort for independence. Support for Latvian statehood was always, not surprisingly, stronger among ethnic Latvians from the beginning: in a 1990 survey, 95% of ethnic Latvians supported secession while 45% of Russian residents did. Support by Russophone residents began to diminish, however, as it became evident that the Latvian Popular Front and the Citizens' Congress would embrace anti-Russophone policies, and the economic consequences of a bid for independence became clearer. A conservative deputy in the Latvian Soviet parliament encapsulated this concern in 1990, in a speech to a crowd protesting against independence:

The example of Lithuania is plainly visible to us. They made a decision in haste, and now suddenly it becomes clear that the cost of independence is \$1 billion a year for oil. And Latvia would need to pay \$1.5 billion. Do we really want a repetition of the Lithuanian alternative? No, in Latvia this will not do.<sup>97</sup>

According to exit polling conducted during the 1990 Supreme Soviet elections, in which Russophones were allowed to vote, ethnic Latvians tended to vote for Latvian Popular Front candidates while Russophones more often voted for opposition parties further to the left.<sup>98</sup> This left-wing and pro-Moscow preference was demonstrated in the 1993 elections to the Russian legislature, in which nearly half of Russian voters in Latvia voted for the Communist Party, and one third for the nationalist, expansionist Liberal-

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<sup>97</sup> Rosen, James "Russians rally against Latvian independence" *United Press International* May 1, 1990. Online. LEXIS-NEXIS Academic Universe.

Democratic Party headed by Vladimir Zhirinovskiy.<sup>99</sup> In the 1995 Russian elections, an even larger portion of Russian voters in Latvia again voted for the Communist Party.<sup>100</sup> According to 1997 survey data, the political position of Russophones in Latvia remained further to the left than that of their Latvian-speaking neighbors. Russian-speakers were more likely to identify themselves as “extreme left” or “left”, while Latvians were more likely to self-identify as “extreme right” or “right”. Russian speakers were also much more likely to state a political preference of a party in the radical left, left liberal or center left, while Latvians on average preferred right-wing parties.<sup>101</sup>

### *Political coalitions*

In Latvia, politics were somewhat more fragmented than in the other globalizer, Estonia, with leftist groups playing a more important role. In Latvia in January 1990, the Supreme Soviet voted to abolish the official “leading role” of the Communist Party. Later that spring, the Latvia Popular Front won a clear majority in legislative balloting, and the then-head of the Supreme Soviet Presidium became head of state. A referendum was held in March 1991, in which over 73% of participants voted for independence. Parliamentary (Saeima) elections were held in June 1993, at which the Latvian Way Union won nearly a third of votes and a plurality of 36 of 100 seats. In July, the Saeima

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<sup>98</sup> Rosen, James “Latvia nationalists in election setback” *United Press International* April 29, 1990. Online. LEXIS-NEXIS Academic Universe.

<sup>99</sup> “Preliminary results of election in regions” *ITAR-TASS* December 14, 1993. Online. LEXIS-NEXIS Academic Universe.

<sup>100</sup> “Majority of Russian citizens in Latvia vote for Communists” *Baltic News Service* December 18, 1995. Online. LEXIS-NEXIS Academic Universe.

<sup>101</sup> Marja Nissinen *Latvia's Transition to a Market Economy* (New York: St. Martin's Press, 1999), pp. 234-5.

elected Guntis Ulmanis of the Latvian Farmers' Union president. Later that month, Latvian Way Union's Valdis Birkavs was confirmed as head of a governing coalition that included Latvian Farmers' Way. This government lasted only a year, however, as the Latvian Farmers' Union withdrew its support in July, 1994 when the government failed to enact protectionist measures on agricultural imports. A proposed coalition with the right-wing Latvian National Conservative Party was rejected by the Saeima, after which a new coalition was approved under Maris Gailis of the center-right Latvian Way Union in September.

Parliamentary elections were again held in September and October 1995, during which the Latvian Way Union lost ground. A fragmented legislature was produced, with 9 parties winning seats and the centrist Master Democratic Party gaining a narrow plurality of 18 seats. This constituted a small move to the left. An attempt to form a leftist conservative governing coalition was rejected. President Ulmanis proposed that nonparty former agriculture minister Andris Skele lead the government. He was approved in December 1995 with a large majority, and headed a center-right eight-party coalition that included the Master Democratic Party, the Latvian Way Union, and moderate conservative parties. The Latvian Unity Party, a conservative collection of largely former communists, often came into conflict with the ruling center-right coalition. President Ulmanis enjoyed the support of most of the coalition parties, and won parliamentary reelection in June 1996 over his master Democratic Party Rival, parliamentary speaker Ilga Kreitse.

This governing arrangement in turn broke down as the largest coalition partner, the centrist Master Democratic Party, attempted to assert itself. In October 1996, Ilga Kreituse was ousted, and both her husband, the finance minister, and the Master Democratic Party deputy prime minister, Cevers, resigned. Prime minister Skele resigned as well in January 1997, but was quickly reinstated, forming another diverse coalition of the Latvian Way Union (center-right), Latvian National Conservative Party (ultra-nationalist), Latvian Farmers' Union (moderately conservative), Master Democratic Party (liberal economics, moderate nationality policy), and Fatherland and Freedom Alliance (ultra right-wing nationalist). This coalition government was committed to reformist economic policies. Skele subsequently resigned again, but the coalition remained intact and appointed Economics Minister Guntars Krasts of the newly-formed Fatherland and Freedom/Latvian National Conservative Party to replace him. Yet despite the many changes in government, the spectrum of coalitions to rule Latvia after independence has been relatively narrow, ranging from far right to center-right. There has been broad agreement across these coalitions on the issues of relations with Russia and the need for greater energy autonomy.

### *Energy and economy*

The economy of Latvia, like those of the other European NIS, was trade-dependent: in 1997, as a percentage of GDP, imports were approximately 49% and exports 47%. Macroeconomic indicators were fairly positive: inflation was 10% for 1997, and GDP growth was about 4%. The Latvian government was interested in joining the

EU and NATO, and was striving to meet Maastricht convergence criteria, despite an initially skeptical reception by the EU. Latvia was largely successful with budgetary austerity, though national politics in general were plagued by corruption charges and discharges of officials and ministers.

Latvia began its economic recovery later than the other globalizer, Estonia. Latvia's GDP stagnated during the 1993-1995 period, after which GDP began to show some signs of growth. It was at the end of this period, in 1995, that Latvia's energy use per capita and per GDP finally bottomed out. Energy trade in general declined greatly, while the development of indigenous energy resources (hydroelectric and wood in particular) increased. The growth of use of domestic energy resources did not entirely fill the gap left by the decline in imports, leaving domestic net consumption in 1996 at 75% of 1992 levels.

Russia remained Latvia's main trade partner, followed by Germany, the UK and Finland. Russia is still Latvia's main energy supplier. However, while Latvia's imports of petroleum and related products from Russia increased by 58% from 1994-95, its imports from Western states increased at a far greater rate: imports from Finland jumped 95%, while Latvia also began to import from new Western sources such as Sweden. As imports from Russia of petroleum oils fell steadily after 1996, they increased from countries such as Finland and neighboring Lithuania. This indicates a strong trend toward diversification of energy imports westward.

Table 4.2 Imports to Latvia: Petroleum Oils (excluding crude), quantity in millions of kg

Exporter	1993	1994	1995	1996	1997	1998
Belarus	208	50	34	52	17	117
Finland	16	97	179	140	109	104
Lithuania	928	229	180	176	133	278
Russia	984	1,154	1,129	1,512	1,069	927
net import	2,848	2,374	1,713	2,093	1,405	1,426

Source: Special report prepared for this project by the Central Statistical Bureau of Latvia, 1, Lacplesa Street, Riga, LV-1301, Latvia, 1999.

Table 4.3 Imports to Latvia: Petroleum Oils (excluding crude), price in Latvian lats per kg

Exporter	1993	1994	1995	1996	1997	1998
Belarus	.044	.082	.113	.109	.112	.053
Finland	.156	.106	.107	.128	.137	.109
Lithuania	.039	.069	.081	.103	.089	.070
Russia	.052	.035	.051	.066	.063	.052

Source: Special report prepared for this project by the Central Statistical Bureau of Latvia, 1, Lacplesa Street, Riga, LV-1301, Latvia, 1999.

Table 4.4 Imports to Latvia: Natural Gas

Exporter:	1993	1994	1995	1996	1997	1998
Russia						
Quantity, 1000 m <sup>3</sup>	943,358	1,010,285	1,202,346	978,400	1,317,760	1,382,000
Lats per 1000 m <sup>3</sup>	54	44	40	46	45.5	43

Source: Special report prepared for this project by the Central Statistical Bureau of Latvia, 1, Lacplesa Street, Riga, LV-1301, Latvia, 1999.

Energy trade reorientation was slower in Latvia than in Estonia. While Latvia began importing oil from non-traditional suppliers almost immediately after independence, these imports as a percentage of the total remain relatively small. Imports of oil from Belarus were closely related to Russian imports, as the crude processed there was supplied exclusively by Russia. Of Latvia's main oil exporters, Finland and

Lithuania<sup>102</sup> provided the strongest diversification of energy supply. Together, Finland and Lithuania accounted for 27% of net oil imports in 1998, again, despite higher prices than those offered by Russia and Belarus. The decline in Latvian oil consumption was substantial. 1998 net import levels were roughly half of those in 1993, which was still substantially less than pre-independence levels. Russia remained the sole source of natural gas for Latvia. Because of the prohibitively high cost of new import infrastructure, Latvia followed Estonia's lead in inviting shared privatization of the sector between Ruhrgas, Gazprom and the Latvian government.

Latvia sought to ameliorate its energy dependence on Russia not only through energy trade reorientation and strategic balancing investment, but also through enhancement of its own domestic resources. Latvia possessed enormous natural gas storage capabilities in underground caverns, which the Baltic state collectively viewed as a potential cushion against shortages for the period that they must rely on a single source: this storage at full capacity could maintain consumption in the three states should Russian supplies be cut, for whatever reason. Latvia also generated electricity through hydroelectric facilities, which it expanded after independence. This potential is volatile, however, as variation in rainfall levels produce variations in energy-generating potential. Latvia also expanded its exploitation of domestic peat and other solid combustibles such as wood. Latvia also imported electricity from Estonia, the supply of which was not dependent on Russia. The volume of these imports varied, of course, based on the volume of electricity generated domestically in Latvia. Latvia sought to make the most of

its severely limited indigenous energy potential, at the same time diversifying its imports toward the other Baltic states and Western Europe. It continued to develop its own resources and build infrastructure (ports and pipelines) to facilitate further energy trade reorientation.

## **VI. Conclusion**

Estonia and Latvia have maintained right-wing or right-center ruling coalitions since independence through political insulation from the economically most vulnerable sector, heavy industry. This insulation was accomplished through the political disenfranchisement of the Russophone residents who form the bulk of the workforce in this sector. This insulation from the most energy-inefficient sector has facilitated the energy trade reorientation of these states from subsidized Russian imports to imports from the West at world market prices. The marketization, economic restructuring, and trade restructuring which have accompanied this have attracted investment and underwritten the economic recovery and subsequent success of these economies, opening for then the door to Western Europe.

The most contentious issue remaining in Estonia and Latvia's EU accession negotiations is the political status of its minorities. The European Union has put pressure on the two states to be more politically inclusive, in accordance with stated European democratic norms, before they can attain full membership. But the demands of "Westernization" and EU accession were somewhat contradictory. In addition to political

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<sup>102</sup> The value of this diversification increases as Lithuania improved its ability to import crude from

democratization and inclusion, economic liberalization, marketization, stabilization and trade reorientation were essential to joining Western Europe. And yet, political inclusion would most likely have brought to power conservative, left-leaning governments, making economic reform and trade reorientation problematic. As we will see in the next chapter, Lithuania responded to these demands very differently. Ethnically homogenous Lithuania, lacking a simple means by which to politically exclude its economically vulnerable sectors, chose inclusion. It also suffered coalitional and policy oscillation, deeper economic crises, and slower progress toward its stated goals of economic stabilization and EU membership.

These conflicting demands of international markets and organizations placed Estonia and Latvia in a difficult position. The Estonian government, for one, has produced a number of new initiatives to improve the economic lot of the residents of the northeast. The strategy seems to be to improve economic conditions in the Russian-speaking areas, so that the residents feel more invested in Estonia's liberal economic policies before they have a chance to influence, and to undermine, them through the ballot box. This irony is not lost on the Russian-speaking residents.

We have now received the European Union report for the Estonian government which asserts that these [citizenship] laws must be changed. Here is such an irony: Russia and the European Union said practically the same thing. But all that comes for the East is [perceived by the Estonian government as] coming from enemies, and all that comes from the West is [perceived as] coming from friends. Now we hope that "friends" may accomplish much more than "enemies" were able to.<sup>103</sup>

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the West.

<sup>103</sup> Interview with author, Leivi Sher, Advisor, United People's Party of Estonia Faction, Estonian Parliament, October 19, 1999.

While the success of Estonia and Latvia's energy trade reorientation, and their ability to maintain pro-market, pro-Western governmental coalitions, in great part rested on their exclusion of the Russian-speaking minorities, it may be just this determination to integrate economically and politically with the West which eventually drives their governments to offer fuller rights and political participation to these minorities.

## **CHAPTER V**

### **HYBRID SYSTEMS: LITHUANIA, MOLDOVA AND UKRAINE**

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#### **I. Summary: The Hybrids and Lithuania**

The hybrid cases have implemented policies that have yielded neither large-scale, sustained energy subsidies from Russia nor advanced energy trade reorientation and economic restructuring. They are often able to maintain lower energy prices than the globalizers receive, but higher than the Russophile has maintained. They have pursued strategic balancing investment and decreasing reliance on imports, and on imports from Russia, with moderate to limited success. Instead, they have found themselves on a middle course in which they face both some energy and economic contraction and many of the most difficult aspects of market forces. In this chapter, I will first examine the case of Lithuania and the coalitional fragmentation and oscillation that produced these strategies. I will then briefly outline the other two hybrid cases, Moldova and Ukraine.

It is somewhat ironic that Lithuania, the place where the independence movement was born, and where the disintegration of the Soviet Union began, lagged behind its Baltic neighbors in terms of reform and economic independence from its former colonizer. Unlike in the globalizers or the Russophile, in the hybrids, no single coalition was able to exert power on a consistent basis. In Lithuania, pro-reform, anticommunist forces came to power in 1990, just prior to independence, but quickly lost the reins of the state to communist forces advocating accommodation with, rather than estrangement from, Russia. Anticommunists were returned to power in 1996, but the enactment of

reform and trade reorientation was delayed and groups dependent on cheap energy remained entrenched.

Lithuania decreased its energy imports from Russia, but, absent a strong right-wing, reformist coalition, was not able to implement the kinds of market reforms that would have yielded it the funds needed to purchase energy at higher prices from the West or fully develop indigenous resources. Lithuania, like the other hybrids, suffered the greatest drop in overall energy consumption. Lithuanian energy consumption in 1997 was 49% of 1991 levels. Furthermore, Lithuania also saw the largest drop in net energy imports as a percentage of total consumption: it dropped by 19 percentage points between 1991 and 1997. It also experienced the greatest drop in net energy imports overall. 1997 net energy import levels were a mere 37% of 1991 levels. Lithuania's economy outperformed those of the other hybrids, but contracted far more than either of the globalizers', to 87% of 1992 GDP by 1997. Like the other hybrids, Lithuania's recovery was slower than in the globalizers: GDP grew by an estimated 5% in 1998.<sup>1</sup> Lithuania, like the other hybrids, made little progress in increasing energy efficiency, with energy use per unit of GDP in 1997 at 90% of 1992 levels. Domestic production of energy in 1997 was roughly on a par with 1992 production at 89%. Imports of energy into Lithuania dropped dramatically in 1992 -- by roughly half -- but remained relatively stable afterward.

As did other hybrids, Lithuania moved to limit its energy dependence on Russia, but was less successful than the globalizers in reorienting its international energy trade

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<sup>1</sup> See chapter three for a fuller discussion.

and domestic economy toward the global economy. Russia remained Lithuania's virtually sole supplier of gas and crude oil. Unable to reorient energy trade away from Russia, right-wing Lithuanian coalitions did their best to let imports fall and fill the shortfall with domestic resources. This was a difficult strategy politically, however, and led to the most dramatic consumption decline among the cases. The subsequent left-wing government sought to reestablish favorable trade status with Russia. Non-monetary payment accommodations were reached with some Russian suppliers, such as the leasing of the Lithuanian Mazeikiu refinery to the Russian LUKoil company in exchange for 20% of production. Lithuania, after the return of the right government, began expanding its oil terminals and seeking Western investors to facilitate energy imports from the West. Russia remained Lithuania's primary energy supplier, however.

While Lithuania actively sought good relations with Moscow, and can be said to have the best relations with Russia of the Baltic states, Lithuania also applied for full membership in both NATO and the EU. While Lithuania did not join the Commonwealth of Independent States, it also lagged behind its globalizer neighbors in acceptance to Western European international organizations. While trade with Germany and other Western European countries grew, Russia remained Lithuania's most important trading partner. Lithuania, like the other hybrids, alternately (and sometimes simultaneously) sought to sustain subsidies from Moscow and to court suppliers abroad, to accommodate Russia and to forge new, sometimes conflicting, alliances. The result has been a tortuous road toward independence and reform.

The other two hybrids, Moldova and Ukraine, were also dominated by political fragmentation and radical changes in ruling coalitions, robbing them of the ability to implement either a consistent globalizer or Russophile strategy. Coalitions in both Moldova and Ukraine displayed initial interest in energy trade reorientation (or at least diversification), but were foiled by political fragmentation and subsequent political swings to the left. Both made slow progress toward diversification while maintaining a close economic and political relationship with Russia. Lithuania lacks the first facilitating condition of the globalizer strategy: it has no substantial, concentrated ethnic minority on whom to foist the costs of energy trade reorientation. While Moldova possesses a substantial and concentrated ethnic minority, this group is highly organized and mobilized, demanding political concessions not through the ballot box but through armed revolt. Ukraine possesses a significant and relatively concentrated ethnic minority, but political exclusion of this group was never enacted. None of the hybrids meet the second facilitating condition: instead of Globalizing coalitions, oscillation and division between coalitions types dominated the politics of these states.

## **II. Independence at a Cultural Crossroads: Lithuanian History and Nation**

Lithuania is the largest and southernmost of the three Baltic states. It has an area of 25 thousand square miles and a population of approximately 3.7 million people. Lithuania is bordered to the north by Latvia, to the east by Belarus, to the south by Poland, and to the west by the Baltic Sea. Its only border with Russia is also to the west, where it meets the Russian exclave on the Baltic of Kaliningrad. Lithuania has perhaps

the strongest history of independence among the European NIS, and yet it is a hybrid rather than a globalizer. Much of its 19<sup>th</sup> and 20<sup>th</sup> century history runs in close parallel with those of the globalizers, while much of its history previous to that was spent merged with the Russophile. While it is both interesting and important to understand the historical origins of the state, these facts mitigate against arguments of historical or cultural determinism.

Like the other cases in this study, Lithuania has been ruled over the centuries by both Western and Eastern empires. Unlike the other cases, however, Lithuania has a quite substantial history of national independence. Lithuania was one of the leading states of medieval Europe, with territories that extended from the Baltic to the Black Sea, merging with Poland in during the sixteenth century. The Lithuanian-Polish empire was ethnically, linguistically and religiously heterogeneous. Catholicism, Orthodoxy, Judaism and Islam were all officially recognized religions. While Lithuanian was widely spoken, a written form of the language was not developed until relatively late (the 16<sup>th</sup> century). Slavonic dialects (most closely related to contemporary Byelorussian) were therefore used in official documents. Polish influence within the alliance gradually grew, and by the 17<sup>th</sup> century Catholicism was becoming strictly enforced.

Present-day Belarus belonged to this medieval empire, playing a prominent cultural and linguistic role within it. During some periods, the histories of Lithuania and Belarus are so conjoined that there is some dispute as to who ruled whom. Some Belarusians argue that this state was less Lithuanian than Belarusian. Indeed, the post-Soviet state symbols of independent Lithuania and Belarus were identical: the knight on

horseback of the Lithuanian Grand Duchy. The parallel and interrelated past of two states with such different presents casts doubt on deep cultural historical explanations for their current circumstances.

Together, Lithuania and Poland ruled a great empire until the eighteenth century, when Lithuania was absorbed into Russia during the partition of Poland. Lithuania, like much of the rest of the European NIS, came under the rule of the Russian Empire during this period. This rule ended in 1915, when the German army took Lithuania in WWI. The Bolsheviks in turn invaded in November 1918 on the heels of the retreating German army. For two months after the German retreat, Lithuania managed to maintain self-rule. However, Vilnius fell to the Bolsheviks in January 1919. The capital was captured in April by the Poles. The city changed hands several more times, but eluded Lithuanian control. Meanwhile, Lithuania moved its capital to the city of Kaunas following the 1920 Polish-Lithuanian armistice that established an independent Lithuanian state.

The struggle for Lithuanian independence of 1918-1920 climaxed in the establishment of a democratic regime in 1920. The fight for independence had been led by the Nationalist Party, which was, much to its own dismay, excluded from power by the newly-elected socialist forces. The Populist-Social Democrat coalition, elected in 1926, was much more ethnically and politically inclusive than the Nationalists had been. In December of that year, the army, led by leaders of the ousted Nationalist Party, staged a successful coup. By 1927, parliament was dissolved and the presidency strengthened. No fewer than 13 attempted coups followed, often initiated by slighted former allies of the ruling president, Antanas Smetona. The regime under Smetona grew increasingly

fascistic. Independent Lithuania came to an end soon following the Molotov-Ribbentrop Pact of 1939, in which Germany and the Soviet Union agreed that Lithuania would belong to the Soviet “sphere of influence.” In 1940, along with Latvia and Estonia, Lithuania was annexed to the Soviet Union.

### *Ethnic homogeneity*

Lithuania was the most ethnically homogenous of the three Baltic states. In 1999, the 3.6 million-person population of Lithuania was approximately 80% ethnic Lithuanian, 9% Russian, 7% Polish, 2% Belorussian, and 2% other minorities.<sup>2</sup> All legal residents at the time of independence in 1991 were granted citizenship. Those who arrived between 1940 and 1991 went through a streamlined registration process. Citizenship was given to residents regardless of their ethnic background or ability to speak Lithuanian. The brand of nationalism adopted by the state in Lithuania was also quite different from those of its Baltic counterparts: it was more inclusive, and more moderate. All residents, including ethnic Russians, were considered to be “Lithuanian,” and were extended citizenship and voting rights. With a relatively small Russian minority, the ethnically-based political exclusion pursued in the globalizers would not have provided the Lithuanian state with much insulation from the political ramifications of economic and energy contraction. From the beginning or “reassertion” of independence in the early 1990s, Lithuania sought to ensure the political rights of all of its citizens, regardless of ethnic origin. In 1989, Lithuania adopted the Law on National Minorities, which guaranteed all citizens (among

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<sup>2</sup> CIA *World Factbook*, 1999.

other things) protection against discrimination, equal protection under the law, as well as providing for education and state services in the minority language in localities where demand is high.<sup>3</sup>

Russification of Lithuanian had been less extensive than in Estonia or Latvia. Whereas industrialization in the globalizers was built in the large-scale immigration of Russians to those republics, in Lithuania, the forced industrialization of the Soviet period was built on the basis on mainly local labor.<sup>4</sup> Thus, the Russian population of Lithuania was a much smaller percentage of the total than in the other Baltic states, and was much less geographically and sectorally concentrated. Perhaps because of this more limited Russification, the share of ethnic Russians who were fluent in the titular language of the republic was already higher in 1990 in Lithuania (37.5%) than it was in either Latvia (22.3%) or Estonia (15%).<sup>5</sup> Of the Russians living in Lithuania, more than half had some knowledge of the Lithuanian language.<sup>6</sup>

Geographical concentration of Russians in Lithuania was less pronounced than in Estonia as well. While there were regions such as Ignalinos (with 47% Russians and Byelorussians) and cities such as Sniekus (with 75% Russians and Byelorussians) with high Russian populations, minority population patterns were less pronounced. The central trend was that they tended to be urban rather than rural. Sectoral concentration was less pronounced than in either globalizer, because industrialization in Lithuania

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<sup>3</sup> "The Law on National Minorities of the Republic of Lithuania" in *The Lithuanian Policy on National Minorities* (Vilnius, Lithuania: Government of the Republic of Lithuania Information Center, 1996).

<sup>4</sup> V. Stankuniene et al., *Demographic Changes and Population Policy In Lithuania* (Vilnius, Lithuania: Lithuanian Sociological Institute, 1995), p. 146.

<sup>5</sup> *Ibid.*, p. 157.

relied much more heavily on Lithuanian labor. Thus, political exclusion of minorities based on ethnicity or linguistic ability, had such laws been enacted, would have done little to mitigate the effects of energy contraction on ruling political coalitions.

### **III. Political Coalitions**

The last round of Soviet-era elections was a victory for the right and opened the door for Lithuanian independence. In the Lithuanian Supreme Soviet elections of February and March of 1990, the secessionist Lithuanian Reform Party (LRP) won a majority of seats. The chairman of the LRP, Vytautas Landsbergis, defeated the Communist incumbent chairman of the Supreme Soviet Presidium, Algirdas Brazauskas in the contest for the chairmanship of the newly-renamed Supreme Council. Landsbergis and the council appointed Kazimiera Prunskiene, a LRP-endorsed Communist, as chairperson of the Council of Ministers. The Lithuanian government immediately declared independence from the Soviet Union. Moscow responded in April 1990 by imposing an economic blockade on Lithuania, including an energy embargo. The council was forced to suspend its declaration of independence on June 29. However, following six months of fruitless negotiations between Vilnius and Moscow, Landsbergis reasserted Lithuanian independence.

However, the Soviet blockade had dire effects on the Lithuanian economy, and on Lithuanian politics. The governing center-right coalition soon encountered resistance to its austere economic policies. On January 8, 1991, Prime Minister Prunskiene was forced

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<sup>6</sup> Ibid.

to resign over unpopular price increases she had authorized, increases which were necessitated by Moscow's fuel and trade embargo. Three days later, Soviet troops occupied government buildings in the Lithuanian capital of Vilnius, precipitating clashes which would result in the deaths of 14 Lithuanians and the wounding of 700 more. Lithuanians refused to participate in the upcoming vote on Gorbachev's Union Treaty, which was to be held in March. Instead, in February 1991, 90% of Lithuanians polled voted in favor of independence from the Soviet Union. Moscow finally accepted Lithuania's (along with Estonia's and Latvia's) independence on September 6, following the failed hard-line coup in August.

While the Lithuanian state had gained independence from Moscow, its government remained embattled at home. President Landsbergis favored immediate and relatively radical economic reform, while parliament was markedly more left-wing and conservative. Landsbergis attempted to overcome this deadlock by increasing the power of the presidency through referendum in May 1992. While a majority of votes cast were in favor of Landsbergis' proposal, the initiative failed due to low voter turnout. The Lithuanian parliament had a succession of three Prime Ministers between the time of Prunskiene's resignation in January 1991 and the legislative elections in October and November of 1992. Albertas Shuminas, who held the prime ministership the longest during this interim, resigned over frustration with the left-wing forces who, he said, inhibited the government's attempts at stabilization and reform.

Lithuania experienced a severe economic downturn in 1990-1992. Energy-intensive sectors suffered the most. Lithuania's 1992 economic decline, and industrial

decline in particular, was one of the worst in the post-communist world. Because of these dire economic conditions, it is perhaps not surprising that Lithuania's first post-independence elections, held in October and November of 1992, were a decisive victory for the left. The Lithuanian Democratic Labor Party (LDLP), the successor to the Lithuanian Communist Party, won a majority in the parliament. Brazauskas, Landsbergis' rival for the presidency and former Communist chairman of the Supreme Soviet Presidium, was elected chairman of Parliament, that is, acting head of state. He was confirmed by direct balloting in February 1993, after which he appointed Adolfas Slezevicius Prime Minister. Less than a year later, however, Slezevicius was forced to resign amid corruption charges related to a banking scandal. He was replaced by Laurynas Stankevicius.

The Lithuanian economy was slow to recover under the socialist government. Economic reforms were slow in coming. Neither full subsidization, such as in Belarus, nor successful marketization, such as in Estonia, was achieved. The accumulation of these economic troubles, and Lithuania's slow rate of economic recovery, took their toll in the next election. The LDLP was ousted in the parliamentary elections of October and November of 1996. The center-right Homeland Union (HU, which had succeeded the RM in 1993) won an overall majority. Other center-right parties also did well in the election. Homeland Union leader and former president Landsbergis was elected chair of the legislature. The HU soon formed a ruling coalition with the Lithuanian Christian Democratic Party (LCDP), a center-right, pro-independence, anti-Communist party established in 1989 as a revival of the pre-Soviet LCDP, which dated back to 1905. Also

included in the coalition government were representatives from the Lithuanian Center Union, a center-right, strongly pro-market reform party. Former Prime Minister Vagnorius was chosen to head the new government.

The HU continued to do well in the local and presidential elections of 1997 and 1998. The HU won 33% of local government seats in 1997, compared with 14% for the LDLP. In a close second-round run-off presidential election, Valdas Adamkus, endorsed by the HU leader Landsbergis, won 50% of the vote, defeating anti-crime former prosecutor Arturas Paulauskas. Adamkus, who had just returned from 30 years living in the United States, ran on an anti-Communist, anti-corruption, pro-Western platform. Prime Minister Vagnorius was reappointed head of a slightly reshuffled cabinet, signaling continuity in the government's emphasis on economic reform and anti-corruption measures.

The victory of the center-right was widely attributed to public frustration with the government and administrative elite still dominated by former Communists, suspicions of corruption by these elites, and the failure of this left-wing government to salvage the economy. The Homeland Union coalition promised to pursue economic reform (while increasing social expenditures and decreasing taxes) and strengthening anti-corruption and anti-crime initiatives. The HU decision to share government power with the Christian Democrats and the LCS was seen as a move to reestablish the broad anti-Communist alliance that had won Lithuania its independence in 1990-1991.

#### **IV. Policy: Hybrid Strategy**

##### *Foreign policy*

While Lithuania actively pursued independence and cooperation with its Baltic neighbors, it simultaneously sought a degree of accommodation with Russia. In July 1991, before Russia's recognition of Lithuanian independence, Landsbergis and Yeltsin signed an agreement allowing Russia rights of transit across Lithuania to its exclave of Kaliningrad. In September 1991, Yeltsin agreed to withdraw Russian troops from Lithuania by the end of August, 1993. The newly-elected leftist government of Lithuania went a step further than did Landsbergis, and signed an energy barter agreement with Russia in March 1993, under which Russia would supply Lithuania with oil, gas and nuclear fuel in exchange for Lithuanian agricultural and manufactured goods. Yeltsin kept his word, moving out all his troops after the election of the left-wing government and before the deadline.

Lithuania's pro-integration stance on Western political and economic structures remained consistent across governments. Even under the leftist government, Lithuania joined the Council of Europe in 1993, became a signatory of NATO's Partnership for Peace in January 1994, signed an association agreement with the European Union in July 1995, and applied for full EU membership in December 1995. (While all three Baltic states applied for EU membership, in 1997 only Estonia was singled out for accession negotiations with the EU.) There were movements who would prefer a turn westward, however. The governing party (the Homeland Union) backed the policy of working

toward joining both the EU and NATO. The government even established a bureau to oversee harmonization of domestic laws with EU standards.

### *Economic policy*

A large and diverse industrial base was built in Lithuania under the Soviet regime. The Soviet-era Lithuanian economy was heavily dependent upon industry, which comprised about 40% of GDP in 1992. This made the Lithuanian economy particularly sensitive to changes in fuel supply. The fuel embargoes placed on Lithuania by Russia during the former's struggle for independence took their toll, and Lithuania suffered one of the steepest industrial declines in all of the former Soviet Union. Industry collapsed in 1992, and by 1996 industry had shrunk 51%, now comprising only 30% of GDP.<sup>7</sup>

Lithuania's primary industries became food processing, light industry, machine-building, and metal-working. The export-orientation of industry also grew, with over 60% of output in sectors such as textiles, clothing, chemicals, motor vehicles, and communications equipment being sold overseas by 1995. The post-independence industrial recovery was uneven, however. Sectors such as machinery, motor vehicles, medical and precision equipment, and metal industries all experienced large drops in sales in 1996. Large increases in sales were seen in the same year by tobacco, clothing, rubber, and electrical equipment.<sup>8</sup> Agriculture was also affected, shrinking from 11.5% of GDP in 1992 to a mere 7.3% by 1994. Agricultural production dropped by 24% in 1992 alone. Agriculture was the second-largest sector in the Soviet-era Lithuania,

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<sup>7</sup> Economist Intelligence Unit *Lithuania: Country Profile 1997-1998*, p. 77.

dropping to third after independence. The agricultural sector subsequently recovered, rebounding to its former 11% of GDP by 1996. Lithuania's main agricultural activities are animal husbandry and the production of cereals, potatoes, vegetables, sugarbeet and flax.

Immediately after independence, in 1992, Lithuania's economic production was dominated by industry (39%), followed by mining and manufacturing (36%) and agriculture (12%). By 1996, however, industry, mining and manufacturing had experienced extensive collapse. The major structural shift in Lithuania's economy has been the growing importance of trade, which grew from 4.5% of GDP in 1992 to 22.2% in 1996, becoming the second-largest sector in the economy.<sup>9</sup>

The economy as a whole was showing signs of recovery from its post-independence depression. GDP growth grew from a negative 38% in 1992 to a positive 3.6% in 1996, while inflation slowed from 1,020% to 24.7% in the same period. Lithuania's economy was based in manufacturing, and was heavily dependent on trade, which comprised roughly 60% of GDP in 1995.<sup>10</sup> Russia remained Lithuania's main trading partner, both in terms of imports and exports. Germany was a distant second, followed by Lithuania's neighbors Belarus and Poland. Russia remained Lithuania's single largest trade partner and primary fuel supplier.

The economic policy of the state differed markedly under the direction of different political coalitions. The period of March 1990 through January 1991 was characterized by a divided state and conflicting economic policies. Right-wing forces, led by Vytautas

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<sup>8</sup> Economist Intelligence Unit *Lithuania: Country Profile 1997-1998*, p. 83.

Landsbergis, formed the majority in the Supreme Council. At the same time, the Communist Party-successor, the LDLP, played an important role in Prime Minister's Kazimiera Prunskiene's government. While the Supreme Council sought to consolidate Lithuanian independence through new, pro-market laws and economic reforms, the government delayed the adoption of these, often neither supporting nor implementing the decisions of the Supreme Council. Instead, the government focused the public's attention on the effects of the Soviet economic blockade, for which it held the pro-independence forces in the Supreme Council responsible. The government was accused by critics of exaggerating the impact of the blockade on Lithuania, and on purposely increasing prices of foodstuffs at the same time that Soviet military pressure on Lithuania was at its apex.<sup>11</sup> This period of divided rule came to an end in January 1991, when Prime Minister Prunskiene was forced to resign.

From January 1991 to October 1992, pro-reform forces controlled both the Supreme Council and the government. During this year and a half, under the government of Vagnorius and Abisala governments, Lithuanian policy was characterized by remarkable economic reforms. The Lithuanian economy was separated administratively from that of the USSR and the movement from a centrally-managed to a market economy was begun: enterprises were granted self-governance; liberalization of prices, including energy prices, was begun; a system of social guarantees was implemented; a national currency (coupons) was introduced; an independent state budget was established;

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<sup>9</sup> Economist Intelligence Unit *Lithuania: Country Profile 1997-1998*, p. 92.

<sup>10</sup> Economist Intelligence Unit *Lithuania: Country Report, 3rd Quarter 1997*, p. 31.

<sup>11</sup> Antanas Buracas, ed., *Lithuania Economic Reforms: Practice and Perspectives* (Vilnius, Lithuania: Margi Rastai, 1997), p. 33.

revisions of the system of centralized resource distribution to enterprises was reformed; and independent relations were established with international institutions such as the World Bank and The IMF.<sup>12</sup> Privatization was begun, and real estate which had been expropriated by the Soviet powers was returned to its previous owners.

These reforms, however, met with stiff resistance. The restructuring of the economy threatened the power of many of the former *nomenklatura* still in politics, and the reformist governments gradually lost the support of the majority of the Supreme Council.<sup>13</sup> Without this support, the government could not adequately influence either the Bank of Lithuania nor the critically important Ministry of Energy, which was dominated by officials loyal to the *nomenklatura* and LDLP. Many heads of collective farms also opposed the reformist governments. In addition, Moscow continued its pressure on the Lithuanian government by blocking payments by making use of its influence in the banking system and by contracting the supply of oil to Lithuania.

While international recognition of Lithuanian statehood, which came in late 1991, looked like it might strengthen the government's hand, this recognition was not accompanied by any financial assistance from foreign countries or institutions at the time. Meanwhile, the economic ramifications of the introduction of market reforms, such as high inflation, were being felt. The LDLP launched a campaign to cast the economic difficulties as failures and incompetence on the part of the reformist governments, rather than as necessary and temporary adjustments to a post-Soviet economy, and called for

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<sup>12</sup> Antanas Buracas, ed., *Lithuania Economic Reforms: Practice and Perspectives* (Vilnius, Lithuania: Margi Rastai, 1997), p. 33.

<sup>13</sup> Antanas Buracas, ed., *Lithuania Economic Reforms: Practice and Perspectives* (Vilnius, Lithuania: Margi Rastai, 1997), p. 34.

early elections. The left-wing LDLP was successful on both counts, and won a majority in the legislature elected in autumn 1992.

The LDLP ruled the newly-formed legislature (Seimas), the successor to the Supreme Council. LDLP leader, Algirdas Brazauskas, was elected president, and LDLP-backed governments under Bronislavas Lubys and Adolfas Slezevicius were established. Under the LDLP, the Lithuanian currency (litas) was established, and later pegged to the US dollar, helping to bring inflation under control. Economic policy under the left-wing LDLP government differed markedly from that of the previous, right-wing reformist governments. The planned privatization of much state-owned property was cancelled. Where privatization did proceed, it was structured to create favorable opportunities for the heads of the enterprises, ministries, and other nomenklatura allies of the LDLP. The prices at which the properties were sold were also usually quite low, robbing the state of revenue. The government also relaxed the hard budget constraints of many enterprises, helping them avoid bankruptcy and increasing the burden on the state budget and on taxpayers. Lithuania's economy began to lag behind those of its Baltic neighbors. The government also suspended reform of the banking system, precipitating a crisis in the years ahead. Economic policy under the LDLP fostered its political supporters, principally members of the Soviet-era communist and bureaucratic elites, while it at the same time undermined many independent small and medium-sized businesses. Unlike in the globalizers, the economic and political structures in Lithuania remained highly integrated with one another.

### *Energy policy*

As in many other Soviet republics, a large and diverse industrial base was built in Lithuania under the Soviet regime. The Soviet-era Lithuanian economy was heavily dependent upon industry, which comprised about 40% of GDP in 1992. This made the Lithuanian economy particularly sensitive to changes in fuel supply. The fuel embargoes placed on Lithuania by Russia during the former's struggle for independence took their toll, and Lithuania suffered one of the steepest industrial declines in all of the former Soviet Union. Industry collapsed by 51% in 1992, and by 1996 industry had shrunk from 40% of GNP to 28%. This was a substantial drop, considering GDP also shrank to 82% of its 1992 level.<sup>14</sup> It is unclear that this translated into great gains in efficiency, however: energy consumption by industry in Lithuania in 1996 was 80% of 1991 levels.<sup>15</sup> In fact, considering the lagging pace of Lithuania's economic recovery, energy consumption levels remained remarkably stable across most sectors.

Table 5.1 Energy Consumption by Sector, Lithuania 1991-1996

	1991	1992	1993	1994	1995	1996	1996 as % of 1992
Industry	2072	3374	1670	1438	1558	1643	49%
Transportation	50	1290	934	827	1189	1261	98%
Agriculture	398	429	352	248	194	183	43%
Public	190	549	596	588	507	472	86%
Residential	1578	1663	1751	1713	1393	1320	79%
TOTAL	11516	7785	5459	4963	5001	5054	65%

Source: *Energy Statistics and Balances, 1992-1996*, International Energy Agency. Measured in millions of tons of oil equivalent (toe).

<sup>14</sup> Economist Intelligence Unit, *Lithuania: Country Profile 1997-1998*, pp. 83-92. See chapter three for a fuller discussion.

<sup>15</sup> Figures regarding industrial consumption of energy for the year 1992 are extraordinarily high, and may indeed be an aberration due to new reporting procedures. 1996 industrial consumption is 49% of the 1992 "spike", but follow a relatively steady trend when compared with 1991 and 1993-95. Comparison with other data sources regarding the 1992 figures is in order before a conclusion can be reached in this matter.

Lithuania was slow to reorient its energy trade away from Russia. There were a number of reasons for this. First, Lithuania's oil refinery and distribution infrastructure was a large employer and an important and component of the economy. Also, unlike in Estonia, where the energy and heavy-industry sectors were dominated by the politically disenfranchised, in Lithuania it was Lithuanian voters who were employed there. The right-wing reformist coalition of the early years began to implement market reforms and pro-Western policies, risking the loss of Russian energy subsidies. The ill-effects of these policies were immediate, dramatic, and unfortunately for the coalition, followed promptly by a round of national elections. The disenchanted Lithuanian population elected a left-wing government that put the brakes on marketization and sought accommodation with Russia instead.

Table 5.2 Natural Gas Imports to Lithuania, all from Russia (thousands of tons)

	1993	1994	1995	1996	1997	1998
volume	1,855	1,072	1,831	1,784	1,633	1,555
litas per ton	340	480	410	440	450	430

Source: *Foreign Trade*, issues 1992-1999, Statistical Department of Lithuania, prie Lietuvos Vyriausybes, Vilnius, Lithuania.

Table 5.3 Crude Oil Imports to Lithuania (thousands of tons)

	1994	1995	1996	1997	1998
volume - Russia	58	3,013	3,672	5,027	6,339
litas per ton - Russia	260	390	430	450	320
volume - Uzbekistan	828	--	--	--	--
litas per ton - Uzbekistan	10	--	--	--	--
net imports	905	3,007	3,549	4,832	6,074

Source: *Foreign Trade*, issues 1992-1999, Statistical Department of Lithuania, prie Lietuvos Vyriausybes, Vilnius, Lithuania.

This brief flirtation with a right-wing coalition was not enough to secure energy trade reorientation, however. Russia remained Lithuania's single largest trade partner and primary fuel supplier. In 1996, Russia purchased 23.8% of Lithuania's exports, and was the source of 29% of its imports. Not surprisingly, first among Lithuania's imports are mineral products – oil, in particular. As of 1998, Lithuania still imported most of its fuels from Russia. Lithuania possessed the only crude-oil refinery in the Baltics, Mazeikiu, the primary supplier for which was Russia. Because of supply problems with Russia, Mazeikiu continued to operate well below capacity. Lithuania was also the most nuclear-dependent country in the world, relying on its Chernobyl-style nuclear power plant, Ignalina, for 83% of its electricity (1996).<sup>16</sup> Nuclear fuel for the Ignalina reactors was also imported from Russia.

The bulk of Lithuania's electricity was generated at the controversial Ignalina nuclear reactors. In 1998, Ignalina generated 77% of Lithuania's electricity, compared with 18% by thermal generators and 5% from hydroelectric sources. Because of the decline in fuel imports from Russia, Lithuania actually became more dependent on nuclear power after independence. The Ignalina facility consisted of two Chernobyl-type reactors. Because of safety concerns and pressure for the European Union, the first reactor was scheduled to be closed by 2005. A decision on the second reactor was to be made by 2004. In 1999, Lithuania generated a surplus of electricity, so the first closure

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<sup>16</sup> Economist Intelligence Unit *Lithuania: Country Profile 1997-1998*, p. 81.

would most affect exports, which would adversely affect countries like Belarus. Belarus, one of Lithuania's most important customers, most often fails to pay its bills.

In 1998, under the right-wing government, Lithuania began construction on new, small hydroelectric plants, in an effort to diversify and ensure supply.<sup>17</sup> That same year, Lithuania sought new export energy markets in the West through partnership with the US consortium Powerbridge. The project was to build lines linking Lithuania to the Polish power grid. While the deal ultimately fell through, the government set the project out to tender again in 1999. However, it seemed unlikely that Lithuania would continue to produce a surplus of energy for long. The question for Lithuania in the future most likely will not be to whom to export electricity, but how to generate enough for domestic consumption.

Table 5.4 Lithuanian Electrical Energy Exports (thousands of MWH)

	1995	1996	1997	1998
Belarus: volume	2,063	2,401	2,718	5,555
Belarus: litas per MWH	65	65	75	80
Latvia: volume	824	1,269	874	172
Latvia: litas per MWH	82	90	70	90
Russia: volume	--	752	638	--
Russia: litas per MWH	--	70	70	--
net exports	2,887	4,550	4,093	5,348

Source: *Foreign Trade*, issues 1992-1999, Statistical Department of Lithuania, prie Lietuvos Vyriausybės, Vilnius, Lithuania.

<sup>17</sup> Lithuanian Energy Institute, *Energy in Lithuania '98* (Vilnius, Lithuania: Lithuanian Ministry of Economy, 1999).

Lithuania last issued its National Energy Strategy in September 1999.<sup>18</sup> Lithuania's long-term energy plan was based on increased consumption of natural gas, like Estonia's. Unlike on crude oil imports, Lithuanian was not able to maintain a substantial discount on natural gas imports from Russia. The planned reliance on natural gas was based in its relative efficiency as a fuel, both in terms of price and pollution. Lithuania must also plan for the possibility that it may not be able to rely on the Ignalina nuclear power plants for its electricity generation. However, security of the gas supply remained an important question, particularly because of the lack of progress on the Baltic Ring project. Natural gas in Lithuania remained a single-supplier fuel. The Baltic Ring project would, in theory, build a pipeline system connecting the Baltic states to Northern and Western Europe, and thus gas to gas supplies in the North Sea. This project remained, like Lithuania's increased reliance on natural gas, entirely theoretical. Perhaps the most practical near-term possibility for Lithuania to secure its gas supply lay in Latvia, or rather, under Latvia. Latvia possessed substantial underground storage capacity for natural gas which, the Baltic states hoped, would someday be filled to capacity and provide them with a one-year buffer against supply interruptions by Russia.

Lithuania had very limited domestic oil resources. Both Latvia and Lithuania asserted claims over a potentially oil-rich region of the Baltic Sea. However, current known oil reserves were very small, estimated at 360 million barrels. Utilization was even smaller: in 1997, Lithuania extracted only 212 thousand tons, in contrast to its

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<sup>18</sup> Lithuanian Ministry of Economy, Vilnius, Lithuania.

imports of over 5.8 million tons.<sup>19</sup> However, Lithuania possessed a large oil refinery complex, and processed fuel products in excess of domestic consumption. It had historically exported that surplus. The Mazeikiu oil complex, as outlined above, was an important employer and facet of the overall Lithuanian economy. Production at the complex suffered greatly under the first right-wing government: oil processing and production fell dramatically in 1991 and 1992. However, in 1993, under the left-wing government and after deals had been secured with Russia, production began to climb again.<sup>20</sup> The left-wing government negotiated more reliable crude oil supplies and price advantages from Russia. These discounts lasted until 1997, after the leftist government was ousted and replaced again with a more right-leaning, pro-Western coalition, when the crude oil discount from Russia began to wane.<sup>21</sup>

After the reelection of a reformist government in 1996, policy toward Lithuanian oil infrastructure underwent a change, in favor of privatization and diversification. The government poured resources into construction of the Butinge oil import terminal. Since Lithuania did not possess the means to completely reorient oil imports from Russia on its own, the reformist coalition in Lithuania sought to emulate the policies of the globalizers by inviting a strategic Western investor to balance Russian influence on the domestic energy industry. In 1998, the government consolidated the oil sector, including the refinery, the oil terminal, and pipeline infrastructure, and put it up for tender.

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<sup>19</sup> Economist Intelligence Unit, *Lithuania: Country Report, 1999-2000*.

<sup>20</sup> Lithuanian Energy Institute, *Energy in Lithuania '98* (Vilnius, Lithuania: Lithuanian Ministry of Economy, 1999).

<sup>21</sup> See chapter two for a fuller discussion.

The refinery at Mazeikiu was still supplied with crude exclusively by the Russian oil company, LUKoil, in 1999. LUKoil wanted to obtain a majority stake in the refinery, and the rest of the oil infrastructure bundled with it. Lithuania instead decided to privatize the domestic oil concerns to an American oil company, Williams. A Russian supplier was still desired, of course, as the existing supply infrastructure was oriented toward Russia. A second Russia oil company, Yukos, took advantage of LUKoil's unpopular stand and bid on the deal, promising reliability of supply and requiring far less control in the enterprise than did LUKoil. LUKoil demanded a great degree of control and minimization of the power of the American company, threatening supply problems if its demands were not met. After the Lithuanian government signed the deal to sell 33% of the Mazeikiu concern to Williams in 1999, LUKoil twice interrupted crude supplies to the refinery. Williams countered with the threat that, since the oil terminal in Lithuania was nearly complete, it would, if necessary, import crude for the refinery from abroad through the terminal. Williams also promised Lithuania large investments to modernize the facilities. In April 2000, the Lithuanian government agreed to sell 10% of Mazeikiu Nafta to Yukos in exchange for its pledge of a steady supply of oil. Yukos was also allowed to export crude directly through Lithuania's terminal at Butinge.<sup>22</sup> In addition, Lithuania began negotiations with Kazakhstan to increase its imports of crude. The fact that this oil was to transit the Russian oil transport system proved the largest obstacle, as

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<sup>22</sup> Radio Free Europe/Radio Liberty *Baltic States Report* V. 1 No. 14 (24 April, 2000). [www.rferl.org/balticreport/2000/04/14-240400.html](http://www.rferl.org/balticreport/2000/04/14-240400.html).

Russia imposed a low annual quota on the amount of oil it would allow Lithuania to import from Kazakhstan through its pipelines.<sup>23</sup>

Table 5.5 Lithuanian Petroleum Oils Exports (thousands of tons)

	1994	1995	1996	1997	1998
Latvia: volume	572	303	738	710	1,467
Latvia: litas per ton	550	610	640	610	460
Russia: volume	1,953	498	709	1,051	515
Russia: litas per ton	150	570	650	680	560
Ukraine: volume	991	446	453	894	933
Ukraine: litas per ton	200	690	800	810	670
Belarus: volume	1,890	14	26	12	41
Belarus: litas per ton	543	1079	844	988	865
net exports	[863]	[80]	473	1,566	2,639

Source: *Foreign Trade*, issues 1992-1991. Statistical Department of Lithuania, prie Lietuvos Vyriausybes, Vilnius, Lithuania.

Lithuania remained a through-station for Russian petroleum exports, as well as a substantial consumer of them. Its imports of energy products from other states remained stable, and in some cases, actually decreased. Lithuanian policy makers under the leftist government sought to maintain energy supplies and subsidies from Russia. They were successful in the area of oil, at least, and managed to increase production again. The right-wing governments, both before and after the left-wing coalition, instead sought

<sup>23</sup> "Lithuania's Hunt for Oil," Radio Free Europe/Radio Liberty *Baltic States Report* V. 1 No. 17 (15 May, 2000). [www.rferl.org/balticreport/2000/05/17-150500.html](http://www.rferl.org/balticreport/2000/05/17-150500.html).

greater energy autonomy from Russia. The first government suffered a great contraction in energy supply, and was ousted because of the larger economic impact of this. The second chose strategic privatization and gradual diversification instead, perhaps hoping to avoid a second, politically disastrous, economic shock.

## **V. Summary of Secondary Cases: Moldova and Ukraine**

### ***Moldova***

#### *History and nation*

Moldova is a land-locked country sandwiched in Eastern Europe between Ukraine and Romania. It is also a small country, consisting of only 13,000 square miles of territory and 4.3 million residents. Like many of the other European NIS, Moldova is ethnically and linguistically heterogeneous: 64% of the population is ethnically Moldovan, 14% Ukrainian, 13% Russian, and 4% Gagauz. The residents of Moldova are predominantly Eastern Orthodox, with a Russian Orthodox minority. The Moldovan language is similar to, some say indistinguishable from, Romanian, which is a member of the Romance group of the Italic subfamily of European languages. Because of its location between South Europe and Western Asia, over its history, Moldova has been the victim of many invasions and territorial conquests. Today, the eastern portion of Moldova consists of the former Moldavian Autonomous Soviet Socialist Republic (now Trans-Dniester), which was a part of Ukraine until 1940. The western portion of contemporary Moldova was Bessarabia, a province of Romania until 1940, when it was incorporated in to the Soviet Union and the Moldavian Soviet Socialist Republic.

The major regional fault lines in Moldova centered around Gagauzia and the Trans-Dniester regions. Gagauzia was populated by a Turkic-speaking people of an Eastern orthodox faith. The majority of the Trans-Dniester residents were Russian, Ukrainian, and other Russophones, though ethnic Moldovans formed a substantial minority of the population (approximately 40% in 1991). The bulk of Moldovan industry, including the generation of electricity (fueled by oil and gas imported from Russia) were also located in Trans-Dniester. Participation in national elections by the residents of these regions was severely constrained, not by the Moldovan central government, but rather by the local secessionist leadership themselves.

In the December 1991 presidential elections, which took place near the height of disagreements between Moldova and the secessionists, only 43 of the 300 planned voting stations in Trans-Dniester were allowed by the local government to open, and all the stations in Gagauzia remained closed. Of the 2.9 million eligible voters in Moldova, fully half a million were denied the opportunity to vote. Snegur's support among the remaining voters was highest in the conservative rural areas, and lowest in the capital Kishinev, where Popular Front and pro-reunification with Romania sentiment ran high among intellectuals.<sup>24</sup>

In 1994, a compromise had been reached with Gagauz leaders for regional autonomy within Moldova. In subsequent parliamentary elections, voting stations operated freely in Gagauzia. Trans-Dniester officials remained stubborn, however, and refused to allow participation in Moldovan national elections on "their" soil. In an

attempt to give residents of Trans-Dniester access in the 1998 parliamentary elections, the Moldovan central government set up a small number of polling stations on the right bank of the river near the Trans-Dniester and arranged to send buses in to collect voters in Trans-Dniester and bring them to the polls. However, on election day, the majority of the buses were stopped by Trans-Dniester forces and turned back, empty. Only approximately 3,000 voters from the Trans-Dniester managed to take part in the elections.<sup>25</sup>

### *Political coalitions*

Moldovan politics since independence have been characterized by division, conflict and disagreement over Moldova's relationship with Russia and its stance on economic reform. These divisions, and the policy inconsistencies which they engendered, undermined Moldova's initial attempts at energy trade reorientation and bound Moldova to Russia's sphere of influence. Moldova remained dependent upon Russia for its energy, particularly oil and gas, and acquiesced to membership in the CIS and its constituent agreements.

In 1989, as anticommunist, anti-Soviet movements swept through Eastern Europe, the Popular Front of Moldova (PFM), a nationalist, pro-independence group was formed in Moldova, and Mircea Snegur was elected chairman of the Presidium of the Moldovan Supreme Soviet. While Snegur was a member of the Communist Party of Moldova, he

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<sup>24</sup> U.S. Commission on Security and Cooperation in Europe report, "Report on the Moldovan Presidential Election, December 8, 1991", December 21, 1991, Washington, D.C.

supported the PFM in its nationalist goals and independence for Moldova. In the 1990 legislative elections, PFM candidates toppled the parliamentary monopoly previously enjoyed by the Communist Party of Moldova. The Communist Party remained a strong force, however, and the resulting legislature was deeply divided. Later that year, Mircea Druc, leader of the PFM and a pan-Romanian nationalist, was appointed chairman of the Council of Ministers. One month later, in June 1990, the Supreme Soviet declared Moldovan sovereignty.

This declaration set off a chain of successions in ethnically-divided Moldova, as Minister Druc's aspirations toward reunification with Romania were perceived as a threat to non-Moldovans in Moldova. In August 1990, the Turkic Gagauz minority declared itself the Republic of Gagauzia. In September 1990, the Russian-populated eastern Trans-Dniester valley announced the formation of the Dniester Soviet Republic. Conflict erupted between the Moldovan government and the secessionist regions, abating only after a threat by Gorbachev to intervene. However, in May 1991, Prime Minister Druc was ousted for his mishandling of the regional problems after having suffered criticism from his own PFM. The pan-Romanian influence on Moldovan policy declined after the demise of Druc, and President Snegur thereafter adopted a pro-independence stance which integrated accommodation with the communist-era power structure.

Following the failed Soviet coup in August 1991, Snegur banned the Communist Party of Moldova and declared the country independent. Snegur was elected president by direct, if uncontested, balloting in December 1991. Because Snegur was the sole

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<sup>25</sup> U.S. Commission on Security and Cooperation in Europe report, "Report on the Moldovan

candidate, the only hope of the opposition to block his presidency was to undermine the 50% voter turnout necessary to elect him. The right-wing opposition, the People's Front of Moldova, called for a voter boycott, which failed. The left-wing opposition in the Trans-Dniester region (and in the equally secessionist Gagauzia) managed to prevent most voting in their territories. Nevertheless, voter turnout in the rest of Moldova was high (83%), and 98% of those voted for Snegur.<sup>26</sup> In the legislature, Snegur was opposed by the nationalist, pro-Romanian PFM, and supported by the pro-independence but non-nationalist *nomenklatura*-dominated Agrarian Democratic Party of Moldova (ADPM). The PFM remained an active opposition force in politics, and managed to block some pro-Russian legislation during the 1990-1994 term, such as ratification of the CIS treaty.

Conflict in the Trans-Dniester region erupted again in March 1992. While Trans-Dniester argued for autonomy within a confederal republic, President Snegur was willing to extend it only special economic status. After a failed attempt at a truce agreement in June 1992, the Prime Minister resigned and a new parliamentary ruling coalition was established which included representatives from Trans-Dniester, under ADPM-member Andrei Sangheli. By February 1994, President Snegur announced his support for substantial autonomy for Trans-Dniester.

The ADPM gained an overall majority in the parliamentary elections in February 1994. In a March referendum, the vast majority of Moldovans voted in favor of

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Parliamentary Elections: Southern Moldova, the 'Security Zone,' and Gagauzia, March 22, 1998", May 1998, Washington, D.C.

<sup>26</sup> U.S. Commission on Security and Cooperation in Europe report, "Report on the Moldovan Presidential Election, December 8, 1991", December 21, 1991, Washington, D.C.

independence from both Russia and Romania. While the ADPM was pro-independence, it also resisted economic reform and marketization, particularly the privatization program initiated by President Snegur in 1995. In response, President Snegur established the party of Revival and Accord of Moldova (PRAM), and argued that greater powers should be given to the executive branch. Nonetheless, the opposition (ADPM)-dominated parliament continued to obstruct Snegur's policy proposals.

In 1997, Snegur faced the ADPM candidate Petru Lucinschi in a run-off presidential election. Snegur represented pro-market and pro-reform policies, in opposition to Lucinschi's left-leaning pro-Moscow and pro-CIS conservatism. Lucinschi won 54% of the vote to Snegur's 46%. This swing to the left continued in the parliamentary elections of 1998, with the rehabilitated party of Moldovan Communists winning a plurality of 40% of seats.<sup>27</sup> The neo-Communist parties of the Agrarian Democrats and the Socialist-Unity bloc, which had held substantial blocs in the previous parliament, did not cross the requisite threshold of 4% of the vote to receive any seats in the new legislature.

### *Energy and economy*

Moldova's economy was primarily agricultural, composed of crops such as of fruits, vegetables, wine and tobacco. The heartland of Moldova's industry, like Estonia's was populated predominantly by ethnic Russians. Whereas this provided Estonia with the means to insulate the state from some of the political consequences of energy trade

reorientation, sectoral restructuring and economic reform, it did not assist Moldova in this way. There are important differences between the cases, however. At the time of independence and the initiation of exclusionary language laws in Estonia, it was ruled by an extremely right-wing, pro-independence, pro-market, anti-Russian coalition. The presence of this coalition made the referendum on voting rights a possibility, and the subsequent exclusion of Russian voters provided a means by which to maintain this coalition. At the time of independence and the height of the Trans-Dniester conflict in Moldova, the state was characterized by fragmentation and disunity, a divided parliament, hobbled by a pro-independence minority, and a pro-independence president who was persuaded to pursue accommodation with Russia for lack of ability to implement decisive, and difficult, reforms.

Moldova's fragmented coalitions were related to its lack of political insulation from the ill effects of the contraction of energy consumption. First, whereas in Estonia the politically-excluded group (Russophones) did not organize nor mobilize to any significant extent, the Russian residents of Trans-Dniester organized, set up their own government, engaged in armed revolt, and used their geographical position to interfere with energy supplies to the rest of Moldova. By force of organization and arms, the population of Trans-Dniester wielded great power in Moldovan politics. In September 1990, the Trans-Dniester Moldovan Republic declared independence. Backed by communists and ethnic Russians and Ukrainians, the Trans-Dniester region established its own government of communists, hard-line former Soviet bureaucrats, and military officers in an attempt to

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*Los Angeles Times*, "World Perspective: Government: Ex-Soviet States Chart Own Course" Carol

secede from Moldova. The government of Trans-Dniester openly supported the hard-line August 1991 coup, and repeatedly sought reunification with Russia proper.

While Trans-Dniester had its own governing bodies, it continued to exert a powerful influence over Moldovan politics. In 1992, shortly after the election of Mircea Snegur to the Moldovan presidency, the Trans-Dniester launched a rebellion, embroiling Moldova in a brief but costly civil war. Approximately 700,000 Trans-Dniester residents took to the streets, resulting in conflicts with Moldovan authorities and hundreds of deaths. Furthermore, 90% of Moldova's power generators and 100% of its power transformers were located in the Trans-Dniester region, and much of the fuel that flows into Moldova from Russia and Ukraine transits Trans-Dniester. The rebels often interrupted the supply of energy as a bargaining tool, and even destroyed some of the pipelines and infrastructure necessary to deliver energy to Moldova. As mentioned above, this rebellion led six months later to the resignation of the Moldovan Prime Minister and his entire cabinet, which was soon replaced by a "government of national accord" which included four representatives from Trans-Dniester. It took the intervention of the Russian government to bring about a cease-fire in 1992. After the 1994 change of government to a more left-wing, conservative Moldovan legislature, compromises were made with Russia to improve relations on the Trans-Dniester issue. These compromises were immediately approved by the newly-elected, left-wing Moldovan government.

The residents of Trans-Dniester held a referendum in December 1995 in which 82.7% of voters cast their ballots in favor of a draft independence constitution and

independent membership for Trans-Dniester in the CIS. Although the constitution was enacted in January 1996, Russia and Ukraine joined Moldova in refusing to recognize the sovereignty of Trans-Dniester. Russia and Ukraine stated that the Trans-Dniester was a part of Moldova, but should have special status within that state. In June 1996, President Snegur of Moldova and "President" Smirnov of Trans-Dniester signed an agreement on Trans-Dniester's status worded vaguely enough to satisfy the demands of both, though the implementation and ratification of the agreement proved more difficult. Trans-Dniester holds its own elections, and elected a bicameral legislature in December 1995 and re-elected Smirnov in 1997. The residents of Trans-Dniester displayed a high level of organization and participation and impacted Moldovan politics even though they often refused to vote in Moldovan elections.

Secondly, whereas Estonia had some indigenous energy sources, specifically, enough oil shale to keep the lights (if not the heat) on, Moldova had all but none. It had virtually no oil, natural gas, or coal resources, and only a limited amount of electric energy production. Since independence, even electroenergy output declined.<sup>28</sup> Moldova's exports of energy products were negligible.<sup>29</sup> Power generation, which was necessary to all sectors of economic life in Moldova, was by far the largest user of natural gas (all of which was imported from Russia), accounting for 50% of consumption in 1993.<sup>30</sup> In addition to this, after 1992, Moldova became a net importer of electricity, relying on

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<sup>28</sup> *Statisticheskii Biulleten'*, Dekabr' 1996, Nomer 23, pp. 60-1, *Mezhhgosudarstvennyi Statisticheskii Komitet Sodruzhestva Nezavisimykh Gosudarstv, Moskva, Rossiia* (Commonwealth of Independent States).

<sup>29</sup> *Statisticheskii Biulleten'*, Avgust 1996, Nomer 16, pp. 98, *Mezhhgosudarstvennyi Statisticheskii Komitet Sodruzhestva Nezavisimykh Gosudarstv, Moskva, Rossiia* (Commonwealth of Independent States).

<sup>30</sup> Robert Ebel, *Energy Choices in the Near Abroad: The Haves and Have-Nots Face the Future* (Washington, DC: Center for Strategic and International Studies, 1997), p. 260.

Ukraine and Russia for 40% of its electricity by 1995.<sup>31</sup> Whereas Estonia had some domestic energy capacity, and soon secured the capital to import more energy from the West, Moldova had none and took much longer to muster the capital for even small purchases from the global market. Moldova could not place on industry the bulk of the burden of energy shortages; all of Moldova, including that populated by ethnic Moldovans, would suffer greatly from such contractions. After enduring the early years of independence, many Moldovans voted for socialist and pro-Russian candidates, producing fragmentation and a subsequent swing to the left.

Table 5.6 Output of Oil, Coal, Gas and Electroenergy, Moldova 1991-1996

	Oil, millions of tonnes	Coal, millions of tonnes	Natural Gas, billion of cubic meters	Electroenergy, billions of kbt
1991	0	0	0	13.2
1995	0	0	0	1.1
1996	0	0	0	1.4

Source: *Statisticheskii Biulleten'. Dekabr' 1996, Nomer 23*, pp. 60-1. *Mezhhgosudarstvennyi Statisticheskii Komitet Sodruzhestva Nezavisimykh Gosudarstv, Moskva, Rossiia* (Commonwealth of Independent States).

In 1994, Pro-Trans-Dniester and pro-“old economy” forces were drawn together in support of the CIS treaty and the lower fuel costs it promised. This did not mean that Moldova did not attempt energy trade reorientation, however. Early in the independence period, Moldova initiated talks with Kuwait, and then with Iran,<sup>32</sup> in an attempt to secure new sources of fuel. Russian import restrictions robbed the already-suffering Moldovan

<sup>31</sup> Robert Ebel, *Energy Choices in the Near Abroad: The Haves and Have-Nots Face the Future* (Washington, DC: Center for Strategic and International Studies, 1997), p. 262.

<sup>32</sup> While Russia remained the sole supplier of natural gas to Moldova, Moldova sought diversification in oil. Moldova eventually signed an agreement with Iran to purchase a small amount of crude oil, to be refined in Romania and Greece and imported to Moldova in 1995 and 1996. Robert Ebel, *Energy Choices in the Near Abroad: The Haves and Have-Nots Face the Future* (Washington, DC: Center for Strategic and International Studies, 1997), p. 261.

economy of the foreign exchange with which it might have purchased oil and gas from other suppliers. Moldova found barter agreements with these states difficult to secure.<sup>33</sup> In 1993, geologists found indications of oil and gas deposits in Moldova. However, Moldova did not possess the resources to explore these possibilities on its own, and sought international investment.<sup>34</sup> The attempts did not amount to much in the absence of a strong globalist coalition necessary to attract or generate capital. After the failed overtures and muddled economic policies of the early independence years, Moldovan politics swung more decisively to the left and accommodation with Russia was reached.

Following the Moldovan ratification of the CIS treaty by the newly-elected leftist parliament in 1994, Russia lowered prices on fuel exports to Moldova and granted it 70 billion rubles, the first installment of a planned 150 billion ruble credit to assist Moldova in paying its energy debts to Russia.<sup>35</sup> The Trans-Dniester region was the most heavily industrialized in Moldova, and accounted for a disproportionate share of Moldova's energy consumption. By 1997, Moldovan debt to Russia for gas totaled \$57 million, over half of which was actually owed by the Trans-Dniester region.<sup>36</sup>

Russia remained the sole supplier of Moldovan gas. Moldova sought diversification in oil.<sup>37</sup> In 1994, Moldova imported most of its mineral products (a category dominated by fuel imports such as natural gas and oils) from CIS members, and

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<sup>33</sup> Radio Free Europe/Radio Liberty, *Newsline* (August 18, 1992) "Moldova Negotiates Oil and Gas Deal with Iran."

<sup>34</sup> Radio Free Europe/Radio Liberty, *Newsline* (September 30, 1993) "Moldova Seeks Foreign Partners for Oil, Gas Prospecting."

<sup>35</sup> Radio Free Europe/Radio Liberty, *Newsline* (August 18, 1994) "Russian, Moldovan Prime Ministers Pleased with Relations."

<sup>36</sup> Radio Free Europe/Radio Liberty, *Newsline* (April 17, 1997) "Moldova Cuts Natural Gas Supplies to Trans-Dniester."

most of those from Russia. Moldova imported 2951 million cubic meters of natural gas, all from Russia. It imported virtually all of its gasoline and heavy fuel oil from Russia as well. The only category in which there was significant diversification was diesel fuel imports, of which Moldova imported 104 thousand tons from Azerbaijan (also a CIS member), compared with 90 thousand tons from Russia. Diesel fuel, however, comprised a relatively small portion of energy imports overall.<sup>38</sup> In 1995, 94% of Moldovan imports of mineral products were still from within the CIS. Again, all natural gas and most petroleum products were from Russia.<sup>39</sup>

Table 5.7 Imports of Mineral Products to Moldova, 1995

from CIS	from non-CIS
US\$367,200,000	US\$23,600,00

Source: *Statisticheskii Biulleten'*, Mai 1996, Nomer 9, *Mezhgosudarstvennyi Statisticheskii Komitet Sodruzhestva Nezavisimykh Gosudarstv, Moskva, Rossiia* (Commonwealth of Independent States).

Table 5.8 Moldovan Major Fuel Imports and Source Countries, 1996-1997

	1996	1997
Total petroleum products	US\$167,665,000	US\$142,403,000
- CIS	US\$150,701,000	US\$142,403,000
- Russia, Ukraine, Belarus	US\$145,200,000	US\$134,853,000
- Russia	US\$74,906,000	US\$92,047,000
Total natural gas (Russia)	US\$118,209,000	US\$120,764,000
Total imports	US\$285,874,000	US\$305,623,000

Source: *External Economic Activities of the CIS Countries 1999*, Interstate Statistical Committee of the Commonwealth of Independent States, pp. 262-263.

<sup>37</sup> *Statisticheskii Biulleten'*, Iuniya 1996, Nomer 11, pp. 130, *Mezhgosudarstvennyi Statisticheskii Komitet Sodruzhestva Nezavisimykh Gosudarstv, Moskva, Rossiia* (Commonwealth of Independent States).

<sup>38</sup> *Vneshneekonomicheskaya Deyatel'nost' Gosudarstv Sodruzhestva v 1994 Godu* (External Economic Activities of the CIS Countries in 1994), Interstate Statistical Committee of the Commonwealth of Independent States (Moscow, Russia: 1995).

<sup>39</sup> *Vneshneekonomicheskaya Deyatel'nost' Gosudarstv Sodruzhestva v 1995 Godu* (External Economic Activities of the CIS Countries in 1995), Interstate Statistical Committee of the Commonwealth of Independent States (Moscow, Russia: 1996).

While natural gas prices remained low, by 1996 price differences for oil imports between CIS and non-CIS suppliers began to diminish. So while Russia remained the sole supplier of natural gas to Moldova, by 1997 some more significant oil trade diversification had begun. In 1996, 89% of major petroleum products (gasoline, diesel, heavy fuel oil and lubricating oils) were imported from Russia and the Russian-supplied refineries in Belarus or Ukraine (half of that directly from Russia). By 1997, this percentage had dropped to 73% (though the volume from Russia had actually increased).<sup>40</sup> In the same period, Romania's share of these imports had increased from 9% to 19%. The relative importance of this diversification is rather small compared with overall imports of these products: natural gas remained approximately 40% of these fuel imports by cash value. Even in 1997, Russia provided 70% of these oil and gas imports, and Russia, Moldova and Belarus together accounted for 84% of natural gas and major categories of petroleum products.<sup>41</sup> Especially considering that Moldova in 1997 imported virtually 100% of its energy inputs (see Table 5.8), Moldova remained substantially dependent upon Russia for its energy, and one of the most dependent of the cases in terms of share of total energy consumption imported from Russia.

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<sup>40</sup> The percentage of imports of these petroleum products from all CIS countries was only slightly higher than that from Russia, Ukraine and Belarus together: 89% in 1996 as opposed to 87%; 77% in 1997 as opposed to 73%. This indicates that other CIS exporters, which might not be supplied with Russian crude, remained small players in the Moldovan market.

Table 5.9 Average Import Prices of Energy Products to Moldova 1995-96

	1995		First Quarter of 1996	
	from CIS	from non-CIS	from CIS	from non-CIS
Coal	37	none	41	none
Gasoline	215	193	199	202
Diesel Fuel	185	188	198	172
Fuel Oil	85	61	107	none
Natural Gas	58	none	58	none

Source: *Statisticheskii Biulleten'*, Avgust 1996, Nomer 16, pp. 103, *Mezhhgosudarstvennyi Statisticheskii Komitet Sodruzhestva Nezavisimyykh Gosudarstv, Moskva, Rossiia* (Commonwealth of Independent States). Units in US\$ per thousand cubic meters for natural gas and in US\$ per metric tonne for all others.

Table 5.10 Imports from Major Trading Partners to Moldova, 1995

	1995, in Millions US\$	as a % of 1994 trade
Russia	278	90%
Ukraine	228.5	186%
Romania	56	131%
Belarus	50.7	252%
Germany	45.6	128

Source: *Statisticheskii Biulleten'*, Mai 1996, Nomer 9, *Mezhhgosudarstvennyi Statisticheskii Komitet Sodruzhestva Nezavisimyykh Gosudarstv, Moskva, Rossiia* (Commonwealth of Independent States)

Moldova was unable to insulate politics from the repercussions of energy contraction, and was forced to seek accommodation with Russia in exchange for continued subsidies. Given Moldova's lack of indigenous resources and total dependence on imports for energy, its underdeveloped economy and its highly organized and vocal pro-Russian minority, it is remarkable that it attempted to seek economic independence and energy trade diversification at all. The wonder is perhaps not that Moldova is not more like Estonia, but rather that it is not more like Belarus.

<sup>41</sup> *Vneshneekonomicheskaya Deyatel'nost' Gosudarstv Sodruzhestva* (External Economic Activities of the CIS Countries), Interstate Statistical Committee of the Commonwealth of Independent States

## ***Ukraine***

### ***History and nation***

Ukraine is by far the largest of the European NIS, with 233 thousand square miles of territory and a population of over 50 million. It is bordered to the north by Belarus, to the east by Russia, and to the west by Moldova, Romania, Hungary, Slovakia, and Poland. Ukraine possesses extensive coastline on the Black Sea, where several ports and the contested Black Sea fleet are located. Ukraine is located on the rich black-earth steppe, one of the most fertile regions on earth. It also possesses substantial natural mineral resources and an enormous, if decaying, heavy- and military-industrial base. The population of Ukraine, like those of the other European NIS, is ethnically mixed, with 71% Ukrainians and 22% Russians. While Eastern Orthodoxy is the predominant religion, there are growing communities of other denominations, particularly Pentecostal Christians. After being ruled by Poland in the sixteenth century, Ukraine experienced a brief period of independence in the seventeenth. In the eighteenth century, however, Ukraine came under the rule of Tsarist Russia. While, following the Bolshevik Revolution and overthrow of the Tsar, Ukraine declared its independence from Russia in 1917, Ukraine was eventually taken by the Red Army and incorporated into the USSR in 1922.

There are clear regional political trends in Ukraine tied to economic and ethnic differences within the country. Western Ukraine, which only came under Soviet control after WWII, was more ethnically Ukrainian, less Russified, and less industrialized than

the southern and eastern portions of the country. The western regions more often supported pro-reform, pro-nationalist, and anti-Moscow candidates and initiatives, while the east and south more strongly supported less economic reform and closer ties with Moscow.

Western Ukraine was the birthplace of the pro-independence movement and the Popular Front of Ukraine (Rukh), and well into the independence period continued to support pro-reform, anti-Moscow forces more strongly than did other regions of Ukraine. Three counties in western Ukraine independently authorized questions on Ukrainian independence during Gorbachev's national referendum on whether to maintain the USSR as a federation in March 1991, a full nine months before the Ukrainian national referendum on independence. In the December 1991 national referendum, the strongest support for independence came from western Ukraine and Kiev, at around 95% of the vote. In contrast, the more heavily industrialized and Russified the region, the weaker the support, with eastern oblasts at approximately 80% and the Crimea, where ethnic Russians predominated, at 54%.

An election for the presidency of Ukraine was held simultaneously with the national referendum on independence. Similar regional patterns emerged. Leonid Kravchuk, former communist boss, incumbent and born-again nationalist garnered 62% of the total vote in a field of seven candidates. His main rival was the more reform-

minded, Rukh-backed Vyacheslav Chornovil. Not surprisingly, Chornovil did best in the oblasts of Lviv, Ivano-Frankivsk and Ternopli, in the western Ukraine.<sup>42</sup>

This pattern continued even until the 1998 parliamentary elections. Conservative communist and socialist parties favoring less reform and closer ties with Russia, such as the CPU, the Socialists and Peasants Party, and the Progressive Socialist Party, dominated in the more heavily industrialized and Russified east and Crimea. The anti-Kuchma, anti-reform party of Hromada gathered its strongest support in Dnipropetrovsk, a heavily industrialized and heavily Russified region. Pro-reform, pro-West and anti-Moscow parties such as Rukh garnered their strongest support in the western regions and in Kiev.<sup>43</sup>

#### *Political coalitions*

In July 1990, the Ukrainian Supreme Soviet, under pressure from pro-independence forces, declared sovereignty, but failed fully to secede from the Soviet Union. Ukraine endorsed Gorbachev's Union Treaty in April 1991, but issued a formal declaration of independence following the failed coup in August. Leonid Kravchuk, then chairman of the Ukrainian Supreme Soviet, suspended the Ukrainian Communist Party. In direct balloting in December, Kravchuk was confirmed as president and the August declaration of independence was overwhelmingly endorsed by the Ukrainian public. Within a week, Ukraine, along with Belarus and Russia, announced the dissolution of the Soviet Union and became a founding member of the CIS. Kravchuk's enthusiasm for the

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<sup>42</sup> U.S. Commission on Security and Cooperation in Europe report, "Ukraine's Parliamentary Election, March 29, 1998" April 1998, Washington, D.C.

CIS was lukewarm, however. Kravchuk viewed the CIS as a temporary structure for the peaceful transformation of the USSR, and speculated that after certain political and economic problems had been resolved, that the CIS would become a purely economic association.<sup>44</sup>

There followed a succession of prime ministers who fell, in turn, over the economic problems inspired by rising prices and the uncertainty of the direction of Ukraine's economic reforms. Among these prime ministers was Leonid Kuchma, the former technocratic director of the Soviet Union's largest arms production complex. Kuchma served as prime minister from October 1992-September 1993. Tensions between the president and parliament nearly led to a constitutional crisis, which was averted only when the two bodies agreed to elections, to be held in early 1994.

President Kravchuk lost to his leftist opponent, former Prime Minister Kuchma, in run-off elections in July 1994. President Leonid Kuchma began his career working in heavy-industry factories and as a member of the Communist Party of the Soviet Union. He worked his way up to the Communist Party Central Committee, where he was a member from 1981-1991. After the fall of the Soviet Union, he served as Prime Minister of Ukraine (1993-1994), and then as Chairman of the Ukrainian Union of Industrialists and Entrepreneurs. His political ties were to industrialists and former Communist Party members.<sup>45</sup> Kuchma's success was due in large part to his backing by the reinstated

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<sup>43</sup> U.S. Commission on Security and Cooperation in Europe report, "Ukraine's Parliamentary Election, March 29, 1998" April 1998, Washington, D.C.

<sup>44</sup> Radio Free Europe/Radio Liberty, *Newsline* (September 7, 1992) "Ukrainian-Russian Treaty in October."

<sup>45</sup> NUPI Centre for Russian Studies Database, [www.nupi.no/cgi-win/Russland/personer.exe](http://www.nupi.no/cgi-win/Russland/personer.exe), Leonid Kuchma, p. 1.

Ukrainian Communist Party and by the strong support by the heavily-industrialized, Russophone eastern regions. Kuchma sought to diversify energy supply, but was constrained by the need to please his industrial supporters who relied heavily upon cheap Russian energy, and found himself severely limited by his shortage of international exchange.

After his election, Kuchma promised economic reform in order to stop Ukraine's downward economic spiral, coupled with greater accommodation with Russia. Kuchma took a very different stand from Kravchuk on relations with Russia and the CIS. Kuchma acknowledged Ukraine's dependence on Russia, but pushed for the strengthening of economic ties and the promotion of freer trade with Russia. Kuchma was also sometimes critical of the CIS, but only because he considered that the CIS Customs Union did not go far enough, and advocated the creation of a free trade zone within the CIS.<sup>46</sup>

Legislative balloting also began in 1994. Because of majoritarian electoral rules, the balloting continued for two years, after which there still remained vacant seats. The Communist Party of Ukraine won the largest bloc. The elections yielded a legislature dominated by the Communist, Peasant, Socialist and Rukh parties. The leftist, pro-Russia, pro-socialist parties formed the dominant coalition. Moderate nationalist, pro-reform, and anti-Russian parties, the largest of which was Rukh, held the second-largest bloc with 35 seats. Rukh, or the Ukrainian People's Movement for Restructuring, which was established in 1988, was the original pro-independence democratic opposition movement. It originally supported Kravchuk, the former president, but after much

internal political turmoil in 1992, came to back Kuchma. The Communist Party backed Kuchma's pro-Russian stand but opposed parts of his economic reform program. A series of crises between Kuchma and the more conservative parliament followed, leading to multiple cabinet reshuffles, struggles for constitutional changes, and no-confidence votes.

Together, the Communist, Peasant, and Socialist parties formed a pro-communist bloc of 118, the largest single group among the 338 seats that were filled.<sup>47</sup> Subsequent rounds of balloting yielded similar results: two years later, when 95% of the seats were finally filled, 160 of the 425 seated deputies constituted a left-wing, Communist-led bloc. The Peasant Party of Ukraine was comprised largely of collective-farm chairmen who opposed radical economic reform and privatization and advocated the preservation of an economic zone within the CIS.<sup>48</sup> The Socialist and Communist Parties also advocated the retention of a large state role in the economy, stronger links with the CIS, and prioritizing the rights and welfare of workers in economic policy. All three parties strongly opposed the Ukrainian nationalist parties who advocated autonomy and departure from the CIS. In fact, the Socialist party called for restoration of the USSR, the reinstatement of communism, and demanded that the Russian language have the same status as Ukrainian

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<sup>46</sup> Radio Free Europe/Radio Liberty, *Newsline* (October 30, 1998) "Kuchma Stresses Economic Ties with Russia."

<sup>47</sup> 112 of the total 459 seats remained unfilled even after the second round of balloting due to a failure of any single candidate to receive greater than fifty percent of the vote, as was required by Ukrainian electoral law. Even two years and countless rounds of balloting later, 25 seats remained vacant.

<sup>48</sup> Political Organizations, [www.brama.com/ua-gov/polorgs.txt](http://www.brama.com/ua-gov/polorgs.txt), Political Organizations, p.5.

in Ukraine. Similarly, the Communists advocated equal rights for all nationalities in Ukraine.<sup>49</sup>

Economic reform came slowly due to vacillations of President Kuchma and the domination of a coalition of Communist and Socialist parties in parliament. The inefficient coal industry suffered from wage arrears, but the state refused to intervene decisively. It was slow to implement restructuring requirements set out by the World Bank, and continued to subsidize production. The workers suffered, but the sector as a whole survived. The state pressed forward with plans for construction of two new nuclear reactors, despite Western analysis that construction would prove financially unfeasible.<sup>50</sup>

Although Kuchma promised greater reform and closer cooperation with the IMF after the disastrous economic years of Kravchuk's rule, his policies continued to subsidize inefficient sectors of the economy. For example, Ukraine purchased its gas from Russia and Turkmenistan. Gas prices to industrial users increased dramatically in 1995 as a result of increased prices from these suppliers. Approximately 6,000 Ukrainian enterprises were cut off from gas supplies shortly thereafter as a result of non-payments. Kuchma decided that the state would assume the enterprises' debt to Russia and Turkmenistan rather than force the closure of inefficient enterprises. (Ukraine's debt to the Russian gas company Gazprom was estimated in 1997 at between \$100 million and

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<sup>49</sup> Political Organizations, [www.brama.com/ua-gov/polorgs.txt](http://www.brama.com/ua-gov/polorgs.txt), Political Organizations, pp.3-5.  
<sup>50</sup> Economist Intelligence Unit *Country Report: Ukraine*, 3rd Quarter 1997, p. 30.

\$150 million.<sup>51</sup>) It was policies like these that led the Communist/Socialist-dominated parliament to give Kuchma the power of decree in the economic sphere.<sup>52</sup>

In 1997, with elections only slightly over a year away, Kuchma attempted to please both the anti-Russian moderate Ukrainian nationalists and the pro-Russian socialist/integrationist bloc. Ukraine and Russia established the Strategic Group on Russian-Ukrainian Cooperation, which was to discuss economic, military, industrial, and energy cooperation. Kuchma sought joint military-industrial projects and an end to Russian taxes on Ukrainian goods, while Russia sought shares in Ukrainian oil refineries. On December 12 1997, Kuchma announced an "end to the economic and political war with Russia," and that Russia would lift some duties on Ukrainian exports. Most importantly, he announced that agreements had been reached assuring gas deliveries through 1998. To assuage the concerns of the anti-Russians, he added that these deals were possible only because "Russia has changed its approach to Ukraine," no longer treating it as a "vassal" but instead as an "economic and political partner."<sup>53</sup>

Ukraine's March 1998 parliamentary elections returned an even more strongly Communist legislature than did the previous balloting. 40% of the seats went to a group of three leftist parties opposed to the president's economic reforms and in favor of closer ties with Russia. The CPU, the largest single seat-holder in parliament, favored a state-run, command-style economy and full reunification with Russia and Belarus. The Socialist and Peasants Party propounded a similar economic agenda, while preferring an

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<sup>51</sup> RFE/RL *NewsLine* 24.07.97.

<sup>52</sup> OECD-IEA, *Energy Policies of Ukraine*, 1996, p. 41.

<sup>53</sup> "Russian-Ukrainian group for closer relations established", NUPI Centre for Russian Studies Database, [www.nupi.no/cgi-win](http://www.nupi.no/cgi-win), p. 1.

active role in the ICS rather than full reintegration with Russia. The final member of the coalition, the Progressive Socialist Party, was stridently anti-reform and considered the furthest to the left. Along with a fourth anti-reform party, the Hromada, this coalition formed nearly a majority of the legislature. The Hromada was formed in 1993 by former Communists. It was revived in 1997 by former Prime Minister Pavlo Lazarenko<sup>54</sup> (who had been sacked by Kuchma in 1997) and former head of the powerful United Energy Systems, in opposition to presidential policies. Hromada advocated a mix of economic policies such as reducing corruption, support for small businesses, and protection of domestic producers from world market forces. Centrists and independents who might be inclined to cooperate with the president comprised about 34% of the seats. Nationalist-democratic reformist parties only received approximately 15%, with Rukh receiving approximately 9% of the seats.<sup>55</sup>

Relations with Russia were troubled. Within Ukraine, two regions, the heavily-industrialized east and the strategically-important Crimea, were heavily populated by ethnic Russians. As in Estonia, the economic sectors which would suffer greatly from energy trade reorientation were populated by ethnic Russians. However, as in Moldova, the state was ruled by fragmented and lame-duck governments, followed by left-leaning, pro-Russian coalitions. If right-wing forces within Ukraine had had the inclination to exclude Russophone residents from the political process, they did not have the political capacity to implement it. The Ukrainian government remained politically accountable to

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<sup>54</sup> At the time of this writing, Lazarenko was in exile in the United States, awaiting possible extradition back to Ukraine to face corruption charges.

<sup>55</sup> U.S. Commission on Security and Cooperation in Europe report, "Ukraine's Referendum on Independence and Presidential Election, December 1, 1991" December 20, 1991, Washington, D.C.

the Russian populations and therefore constrained by the dire economic consequences energy trade reorientation would have posed.

### *Energy and economy*

Ukraine's economy was relatively diversified. Its highly fertile "black earth" region was the bread basket of the USSR. Important agricultural outputs included meat, milk, grains and vegetables. It also had an extensive base of heavy industry that supplied equipment and raw materials to industrial and mining sites in other regions of the former USSR. Ukraine remained largely within the shadow of the Russian economy after independence. Rather than embrace this dependence as Belarus did, however, Ukraine sought to ameliorate it through increased energy independence, though it achieved little success. Ukraine attempted to develop its domestic coal reserves and to enhance the output of its nuclear energy plants. Investment capital for these projects proved problematic, ensuring energy dependence on Russia for some time to come. Chernobyl-type reactors (and Chernobyl itself) continued to function, and strikes in the coal sector continued. Ukraine sought a degree of energy trade diversification after independence: in exchange for Ukrainian nuclear reactor technology, ostensibly for civilian purposes, Ukraine was offered and accepted a deal from Iran for a limited quantity of cheap oil and Iran's assumption of some of Ukraine's energy debt to Turkmenistan. Such moves could not be interpreted as Ukraine shunning Russia, as Russia is the broker and third party in the nuclear technology deal.<sup>56</sup> But they did demonstrate Ukraine's desire to find

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<sup>56</sup> Economist Intelligence Unit *Country Report: Ukraine*, 3rd Quarter 1997, p. 29.

alternatives to dependence on Russia's energy exports. Many of Ukraine's attempts at diversification were frustrated by its lack of capital and its own political will, however, and it remained highly dependent upon Russia.

Shortly after independence, Ukraine sought energy trade diversification. In April 1992, Ukraine and Iran discussed imports of oil from Iran, the construction of a new oil terminal in Odessa, construction of new oil and gas pipelines, and the eventual import of natural gas from Iran as well.<sup>57</sup> While Ukraine was in an enviable position of occupying Russia's main oil and gas export route to Western Europe, thus giving Ukraine leverage in shipment and rate negotiations with Russia, that position was soon undermined by the Yamal pipeline project. In 1993, Russia, Poland and Belarus announced an agreement to build a new gas pipeline system between Russia and Europe which was to circumvent Ukraine.<sup>58</sup> Ukraine would no longer have a monopoly on Russian export routes to the region.

Ukraine also reached out in 1993 to NIS in Central Asia, seeking import agreements with Uzbekistan for natural gas, Kazakhstan for oil and gas,<sup>59</sup> and Turkmenistan for gas. Turkmenistan and Ukraine reached an agreement whereby Ukraine would receive 29 billion cubic meters of natural gas in 1993 (25% of Ukraine's gas requirements). By 1994, about 34% of Ukraine's gas imports were purchased from Turkmenistan. Ukraine had difficulty keeping up with payments to Turkmenistan, and

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<sup>57</sup> Radio Free Europe/Radio Liberty, *Newsline* (February 25, 1992) "Ukrainian-Iranian Oil Deal" and (April 30, 1992) "Ukraine, Iran Reach Agreement on Oil Supplies."

<sup>58</sup> Radio Free Europe/Radio Liberty, *Newsline* (September 1, 1993) "Kuchma Critical of Polish-Russian Pipeline."

<sup>59</sup> Radio Free Europe/Radio Liberty, *Newsline* (February 23, 1993) "Ukraine Bolstering Economic Ties with Central Asian States" and (February 26, 1993) "Kuchma Concludes Central Asian Visit."

soon became Turkmenistan's largest debtor. Turkmenistan cut shipments briefly in 1993 for nonpayments, and again for a more extended period of time in 1994. Ukraine had paid only \$3.4 million of its \$154 million gas bill for 1994, and had racked up a gas debt of over \$700 million to Turkmenistan. In 1994, Russia still supplied 60% of Ukraine's natural gas.<sup>60</sup>

Ukraine also sought to decrease dependence on Russia by increasing domestic production of fuel and energy. In 1993, the government announced its intention to raise the output of oil by 20% and gas by 40% by the year 2000. In 1993, it hoped to buy only 90% of its oil and 60% of its gas from Russia.<sup>61</sup> In 1995, the government approved a proposal to increase oil drilling off Ukraine's southern coast in the Sea of Azov and the Black Sea.<sup>62</sup> However, Ukrainian domestic energy production continued to decline (to 71% of 1991 levels by 1997), and increased only modestly as a share of overall consumption (from 46% to 54% between 1991 and 1997), but only because consumption had dropped precipitously to 61% of 1991 levels. (Table 3.11).

Table 5.11 Output of Oil, Coal, Gas and Electroenergy, Ukraine 1991-1996

	Oil, millions of tonnes	Coal, millions of tonnes	Natural Gas, billion of m3	Electroenergy, billions of kbt
1991	4.9	136	24.3	279
1995	4.1	83.8	18.2	194
1996	4.1	69.6	18.3	185

Source: *Statisticheskii Biulleten', Dekabr' 1996, Nomer 23*, pp. 60-1, *Mezhgosudarstvennyi Statisticheskii Komitet Sodruzhestva Nezavisimykh Gosudarstv, Moskva, Rossiia* (Commonwealth of Independent States).

<sup>60</sup> Radio Free Europe/Radio Liberty, *Newsline* (February 21, 1994) "Turkmenistan Again Threatens to Turn Off Gas", (February 22, 1994) "Turkmenistan Turns Off Gas to Ukraine" and (March 9, 1994) "Ukraine's Energy Situation."

<sup>61</sup> Radio Free Europe/Radio Liberty, *Newsline* (July 15, 1993) "Ukraine Plans Increase in Oil and Gas Production."

<sup>62</sup> Radio Free Europe/Radio Liberty, *Newsline* (November 15, 1995) "Ukraine to Expand Oil, Gas Industries."

Table 5.12 Output of Natural Gas in Ukraine, 1990-1995 (billions of cubic meters)

1990	1991	1992	1993	1994	1995
28.1	24.3	20.9	19.2	18.3	18.1

Source: *Statisticheskii Biulleten', Iuniya 1996, Nomer 11*, p. 125. *Mezhgosudarstvennyi Statisticheskii Komitet Sodruzhestva Nezavisimyykh Gosudarstv, Moskva, Rossiia* (Commonwealth of Independent States).

Of the European NIS, Ukraine possessed by far the greatest store of energy resources. It also had the greatest demand, which far outpaced domestic supply. While output in all energy sectors contracted since independence, it remained substantial. Ukraine had little oil, but did possess and produce a considerable amount of coal, natural gas, and electric energy. Output of these fell after independence, however.

Table 5.13 Consumption, Exports, and Imports of Natural Gas in Ukraine 1992-1994 (in billions of cubic meters)

	1992	1993	1994
Consumption	111.1	99.4	87.3
Exports, to CIS	0.3	0	0
Imports, all from CIS	90.5	80.2	69.0

Source: *Statisticheskii Biulleten', Iuniya 1996, Nomer 11*, p. 128-32. *Mezhgosudarstvennyi Statisticheskii Komitet Sodruzhestva Nezavisimyykh Gosudarstv, Moskva, Rossiia* (Commonwealth of Independent States).

By 1994, Ukraine was importing 31% of its natural gas from Turkmenistan, and the balance (69%) from Russia. Oil imports to Ukraine continued to be dominated by Russia, however; Russia was the source of virtually all heavy fuel oil and 85%-97% of oil products such as crude oil, gasoline and diesel. These percentages were even higher if

imports from Belarus (which imports its crude from Russia) are included: 91% to 97% of major oil product imports were from Russia or Belarus.<sup>63</sup>

This dependence on Russian energy imports continued. In 1996 natural gas imports from Russia alone accounted for 46% of total mineral product imports. In 1997, that share had increased to 56%. Natural gas imports accounted for approximately half of all Ukrainian imports from Russia, and by 1997 exceeded the total value of Ukrainian exports to Russia. While imports of crude oil from Kazakhstan grew through 1997, Russia remained the dominant exporter of crude by nearly two to one. Ukraine imported the vast majority of its processed petroleum products from Russia and Belarus. By 1997, imports of natural gas from Turkmenistan had begun to decline, shrinking to only about 5% of Russian natural gas exports to Ukraine.<sup>64</sup>

Divided government undermined pro-globalist forces' attempts at increased energy autonomy. This government was replaced by a swing to the left, drawing Ukraine further back to the Russian fold. Politics remained divisive, however, precluding strong and consistent energy strategy. While Ukraine eventually achieved limited diversification in its oil and gas, it failed to increase domestic production as a means of decreasing dependence on energy imports from Russia.

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<sup>63</sup> *Vneshneekonomicheskaya Deyatel'nost' Gosudarstv Sodruzhestva v 1994 Godu* (External Economic Activities of the CIS Countries in 1994), Interstate Statistical Committee of the Commonwealth of Independent States (Moscow, Russia: 1995).

<sup>64</sup> *Vneshneekonomicheskaya Deyatel'nost' Gosudarstv Sodruzhestva* (External Economic Activities of the CIS Countries), Interstate Statistical Committee of the Commonwealth of Independent States (Moscow, Russia: 1999).

## **VI. Conclusion**

The hybrids were forced to navigate a path somewhere between radical economic reform and embracing energy dependence on Russia. Unable to maintain a consistent, or sometimes even cohesive, right or left coalition in government, economic and energy policy alternated between reformist and reactionary, sometimes displaying aspects of both. These policies have led to the least successful medium-term economic outcomes of the European NIS cases. While the globalizers were well on their way to recovery and reform, and the Russophile had managed to maintain the status quo to a great extent, the hybrids experienced steady drops in GDP and continued substantial dependence on Russia for energy.

However, the political inclusion which contributed to these states' inability to implement a consistent (if unpopular) economic and energy program may be a value in itself. While Estonia and Latvia denied large portions of their populations the right to vote and Belarus regressed into authoritarianism, Lithuania, Moldova and Ukraine sought to establish inclusive, democratic forms of government. Lithuania and Ukraine succeeded to a very great extent. Moldova pursued integration and representation of its ethnic minorities even in the face attempts at secession of the Trans-Dniester and Gagauz region and obstruction of voting by these local "authorities." And even though the will of these minorities did not impinge on the Moldovan government through the ballot box, their organizational strength and mobilization did make the Moldovan government accountable to them in its policy-making.

What economic and energy policy options are available to a state which must be fully accountable to the “losers” under reform? Lithuanian policies after 1996 were different from those which had gone before and different from many reforms in the globalizers. The new coalition was not far-right, but rather center-right, and pursued a gradualist approach to privatization and reform with special attention to avoiding the economic displacement of the early days of independence. For the energy-dependent NIS, this approach to marketization and energy independence, while it risks obstruction by entrenched interests and reversal by subsequent coalitions, may be the one of the few sustainable policy approaches in a state fully, democratically accountable to those displaced by a transition to a market economy. Other outcomes are equally possible, however. As I have emphasized, the interests of the state, including marketization, cannot simply be assumed. Coalitions of entrenched interests and rent-seekers may capture the state, driving the country to become a perennial hybrid, a stable, if troubled, state not “in transition” to anything. Oscillation of power between conflicting coalitions may produce muddled policies, and the same unhappy result. Special attention should be paid to the outcomes of this approach, as other hybrids search for paths out of their economic quagmires and energy dependence.

## CHAPTER VI

### EMBRACING THE RUSSIAN FOLD: BELARUS

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#### I. Summary: The “Russophile” Case of Belarus

Belarus the clearest case of the “Russophile” outcome. Because Belarus is relatively ethnically homogenous and its heavy industry is widely populated by ethnic Byelorussians, it lacks the first important condition to be a globalizer. Continued domination by left-wing conservative, pro-Moscow, pro-industrialist coalitions mean it lacks the second important condition as well. The dominant coalition in 1990 in the legislature was comprised of conservative social forces tied to old, inefficient industries. This coalition was able to largely deadlock the pro-market efforts of nationalist leader Supreme Soviet Chairman Stanislau Shushkevich and the minority Belarusian National Front in the legislature, leading to Shushkevich’s removal in 1994 and the election of the radically pro-Russian president Alexander Lukashenka. Legislative elections were finally allowed in 1995, not surprisingly yielding a very conservative left-wing parliament.

This coalition espoused a community of interests between the Belarusian and Russian peoples. After independence, Belarus began to move closer to economic and political reintegration with Russia. Of all the cases, Belarus’s energy consumption has suffered the *smallest* decline, because of the continuation of cheap imports from Russia. In Belarus, 1996 energy consumption levels are a full 76% of 1991 levels.<sup>1</sup> This has

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<sup>1</sup> International Energy Agency, *Energy Statistics and Balances of Non-OECD Countries, 1992-1993, 1993-1994, 1994-1995, 1995-1996.*

meant that relatively less economic restructuring has had to take place on the basis of correcting energy-use inefficiencies. Because many of the economic structures remain virtually unreformed, the system suffers from much of the same inefficiency and corruption it did under the Soviet Union. In fact, industrial energy consumption actually *increased* by 26% in 1996 over 1992, despite a sharp drop in GDP. GDP declined in 1996 to 70% of 1992 output, well below average for our cases.<sup>2</sup>

Relatively little privatization and economic restructuring have taken place in Belarus. Industry remained the dominant sector, particularly heavy industry. While the quality of industrial goods does not meet world-market standards, Belarus managed to secure barter agreements with some Russian energy suppliers by which Belarus may purchase its oil or natural gas in exchange for its industrial products. Russia has agreed to sell many energy products to Belarus at the same low prices for which it sells the energy to its own domestic consumers. While in fact the prices are often higher than agreed, the prices are still well below world-market values. Even so, Belarus has often had trouble meeting its payment obligations. Russia has been remarkably tolerant of Belarus' mounting energy debts. As mentioned above, some energy is sold to Belarus for payment in kind. In addition, the Russian and Belarusian states have agreed to broad debt swaps, debt-for-equity swaps, and simple debt forgiveness. Russia remains Belarus' primary energy supplier, and while consumption has contracted, the drop in energy use has not been as dramatic as in other NIS.

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<sup>2</sup> International Energy Agency, *Energy Statistics and Balances of Non-OECD Countries, 1992-1993, 1993-1994, 1994-1995, 1995-1996*.

Belarus has sought to cement this relationship with Russia not only by joining both the Commonwealth of Independent States and a customs union with Russia and Ukraine, but also by seeking full economic and political reintegration with Russia. Unlike many other NIS of Europe, Belarus has not sought full membership in NATO or in the EU. Because of Belarus' failure to fulfil its promises of economic reform, both the World Bank and IMF have withdrawn offers of aid and assistance.

## **II. Dual Heritage: Belarusian History and Nation**

Belarus is a small, land-locked country in the plains of east central Europe. Belarus borders Ukraine to the south and Lithuania and Latvia to the north, Poland to the east and Russia to the east. Belarus occupies approximately 80,000 square miles of relatively flat, relatively resource-poor territory. Of its 10.4 million citizens, approximately 78% are ethnic Byelorussians, 13% Russians, 4% Poles, 3% Ukrainians, with small numbers of Jews and others.<sup>3</sup> The argument has been made that Belarus chose its post-Soviet Russophile path because it is, for all intents and purposes, indistinguishable from the larger Russia and that it has no identity of its own. This argument lies in the assertions that there is no distinction between the two languages and national consciousnesses; that Belarus is culturally authoritarian and anti-democratic; that Belarus has spent more of its history united with Russia than other NIS; in short, that Belarus is historically and inherently "Eastern" and "Russian." To the contrary, over the centuries, Belarus has belonged to empires of both the East and West. While the

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<sup>3</sup> Central Intelligence Agency, *World Factbook*, 1999.

language and the bulk of the population are Slavic in origin, Belarus has spent scarcely more time under Russian rule than some of its non-Slavic neighbors, such as Lithuania. Indeed, its history is closely tied to Lithuania, not a Russophile but a hybrid.

### *Between East and West*

While Russian influence on Belarus has been substantial, Belarus also incorporated Western political, religious, and cultural traditions through its merger over the centuries with other empires such as those of Poland and Lithuania. Many regions of Belarus, particularly in the west, were deeply integrated into the Polish Empire and Catholic traditions. Furthermore, Belarus' resistance to Russian rule is evidenced by repeated campaigns for national independence and its linguistic and cultural distinctiveness proven by deliberate, explicit Russian, and then Soviet, campaigns to extinguish the Belarusian language and culture, to Russify Belarus. What would be the purpose of such campaigns if a population were already "Russian"? Lastly, the historical evidence does not bear out the assertion that Belarus was necessarily more or less culturally autocratic than its neighbors, as it in fact chose to establish a relatively democratic form of government during its brief existence as an independent state during the interwar years.

Belarus was part of the greater Kievan state from the 900s AD. The invasion of the Mongols in the 13<sup>th</sup> century led to the division of the Kievan principalities into West, South, and North-East Russia, which subsequently came to be known as Belarus, Ukraine and Russia, respectively. Belarus sought security from the Mongols and then the

Teutonic Knights through unification with Lithuania.<sup>4</sup> From the 13<sup>th</sup> to the 16<sup>th</sup> century Belarus was at the center of the medieval polyethnic state of the Grand Duchy of Lithuania, Rus and Samogitia, which encompassed the territories of contemporary Lithuania, Belarus, Ukraine and parts of Russia. Belarus was no mere vassal state of Lithuania, but rather influenced the path and culture of the Duchy. Byelorussian was adopted as the national state language. Belarusian culture and language flourished, influenced by and in turn influencing Lithuanian culture. Legal documents, archives and the first bible of the realm were all in the Byelorussian language. The early 16<sup>th</sup> century is often celebrated as the Golden age of Belarusian culture and literature, spawning many of Belarus' most revered writers. Over time, Catholicism became the official religion, penetrating Belarusian culture and supplanting Eastern Orthodoxy. In the 16<sup>th</sup> century, the territory fell to Poland, which carried the Uniate (Eastern Catholic) church to Belarus and Latin as the official language of record.

Only after the fall of the Polish Kingdom and its division among the Prussian, Austrian and Russian empires in the late 1700s did Belarus, along with Lithuania, fall to Russian rule under Catherine II. Belarus and Lithuania were bundled together into a single administrative unit of the Russian Empire called the Northwest province. At the time of Belarus' integration into Russia, most of its people belonged to the Uniate Church, a denomination allied with Roman Catholicism. While the religion had been forced on the Belarusian people by the Poles, it had taken root. After the Russian takeover, Orthodox Christianity was in turn forced on the Belarusian people.

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<sup>4</sup> Ivan Lubachko, *Belorussia Under Soviet Rule, 1917-1957* (Lexington: University of Kentucky

Integration into the Russian Empire met with resistance in the new territories, however. A campaign for national liberation in Poland, Lithuania and Belarus, led by the Belarusian nobleman Tadeusz Kosciuszko, broke out in 1794. The uprising was suppressed by the Russian authorities. Resistance to Russian rule continued to manifest itself in Belarus over the following centuries. Many Belarusians, gentry and peasants alike, fought with Napoleon against the Tsar during the invasion by the former. A second campaign of national liberation erupted in November 1830, and included not only West Belarus but Poland, Lithuania and Western Ukraine. Again, the uprising was suppressed by the Russian military. A third unsuccessful campaign of national liberation was launched by Kastus Lalinousky in 1863-64.<sup>5</sup>

The Belarusian political party, the Socialist Union (Hramada) promoted Belarusian culture and language, took advantage of the October Revolution and collapsing Romanov empire to pursue independence for Belarus. In December 1917, the All-Belarusian Congress opened in Minsk. While under German occupation, Belarus declared independence from Russia in March 1918. The All-Belarusian Congress Executive Committee declared the creation of the independent Belarusian People's Republic, and guaranteed its citizens the right to vote, freedom of speech, of press and of assembly. However, in May of that year, the Bolsheviks signed the peace treaty with Germany at Brest-Litovsk, allowing the latter to annex Belarus. Belarus was unable to hold on to power, weakened by the destruction wrought by the retreating German troops,

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Press, 1972).

<sup>5</sup> Uladzimir Novik, *Belarus: A New Country in Eastern Europe* (Minsk, Belarus: Technalohija Publishing Company, 1994).

and was taken by the Red Army again in 1919. The reign of the short-lived republic ended, and the government was driven into exile. Again, Belarus was merged with Lithuania, this time under Soviet rule, into the Soviet Republic of Litbel.

The Russo-Polish war soon broke out, however, resulting in the division of Belarus into West (including Vilnius, now Lithuania), which was integrated into Poland, and East, which eventually became the Belarusian Socialist Soviet Republic. In March 1921, at Riga, Lenin ceded West (Brest and Grodno regions) Belarus to Poland, under whose control it remained until 1939. This territory (minus the Vilnius region, of course) was reunited with Belarus in 1939 under the conditions of the Molotov-Ribbentrop Pact. Belarus was virtually destroyed during WWII. The capital, Minsk, was razed to the ground (95% of its buildings were flattened during the war), and a full quarter of the Belarusian population perished. In addition to the horrors of Hitler's armies, the Belarusians suffered at Stalin's hands as well. Tens of thousands of Belarusians were murdered in the Belarusian forest, and many more were sentenced to the gulag or exile. Belarusian nationalists were special targets of Stalin's wrath.

### *The (re)population of Soviet Belarus*

Under Soviet rule, Belarus underwent rapid industrialization. In 1959, Belarus had the 2<sup>nd</sup>-highest proportion of collective farmers of any Soviet republic (second only to Moldova) at 53% of the population. Moscow settled many skilled Russian workers in Belarus to help rebuild after the war, to industrialize Belarus, and to replace the Belarusians and Jews who had been slaughtered there. By 1990, only 20% of Belarusian

citizens worked in agriculture. The Belarusian population had become highly industrialized and urbanized.<sup>6</sup> Along with the Soviet campaign of industrialization came the campaign against the Belarusian language and culture. Like the Tsars of previous centuries, the rulers in Moscow sought the Russification of Belarus. Instruction in schools promoted the use of Russian over Byelorussian, especially in urban areas. Russification also took place in publishing, public life, the work place, etc., where the Soviet regime forced a change to the Russian language. These deliberate campaigns presupposed at least a perceived distinction between the Russian and Byelorussian languages. Despite the Soviet policies, however, and despite the fact that over time Russian did become the *de facto* language in the cities of Belarus, as late as 1989, 80% of Belarusian citizens identified Belarusian as their native language.<sup>7</sup>

Belarus enjoyed some of the best jobs, highest economic growth, industrial output and annual increases in labor productivity in the USSR. Belarusian society was equally privileged: educational standards, infant and maternal mortality rates compared with those of Western Europe. The argument has been made that the relatively privileged and prosperous positions of the Baltic states within the Soviet Union influenced their choice of marketization in the post-Soviet period. The case of Belarus -- highly privileged, and yet the strongest "Russophile" among the cases -- presents a formidable counterexample to this logic.

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<sup>6</sup> Karen Dawisha and Bruce Parrott, *Democratic Changes and Authoritarian Reactions in Russia, Ukraine, Belarus and Moldova* (New York: Cambridge University Press, 1997), p. 234.

<sup>7</sup> *Ibid.*, p. 235.

The post-Soviet composition of Belarusian society was somewhat mixed, as it was in most of the NIS. Religious expression experienced a revival in Belarus. Orthodox Christian churches reopened, and formed the largest number of churches. However, Catholic and Baptist denominations, “Western” religions, were the fastest-growing faiths in Belarus. As of 1998, there were approximately 1,000 orthodox congregations in Belarus, compared with approximately 400 Catholic congregations. While Belarus was predominantly Byelorussian, there were small Polish and Russian minorities. This measure of diversity, religious and ethnic, had a regional dimension as well: the Western regions, which experienced a greater Polish influence, were more Catholic and more Polish, less Orthodox and less Russian than the eastern and urban areas.<sup>8</sup>

Like Lithuania, Belarus is relatively ethnically homogenous. In 1989, nearly 80% of the population was ethnic Byelorussian. The largest minority in Belarus, as in the other European NIS, was Russian. Russians, who comprised roughly 13% of Belarus’ population, lived predominantly in the cities and towns of the eastern regions of the country.<sup>9</sup> Poles made up 4% of the population, the second largest minority. The bulk of the Poles lived in the Grodno region, in the far west of Belarus.<sup>10</sup> While there was therefore some difference between the more agricultural, Catholic and Polish west and the more industrial, orthodox and Russian east, unlike in the globalizers, Byelorussian workers predominated in every sector of the economy. The ethnic minority was too small and sectorally dispersed to meet the necessary condition of the globalizers.

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<sup>8</sup> Dr. Nina Antonovich, “Belarus: A Divided Country” (unpublished manuscript), Belarusian State University, Minsk, Belarus, 1999, p.3.

### III. Political Coalitions: Consolidation of Left-Wing Conservatism

In many ways, the political landscape in Belarus changed little during its first nine years of independence. In the Belarusian capital of Minsk, not far from the intersection of Komsomol and Karl Marx Streets, sat the imposing building of the KGB. The bureau, like many of the streets around it, was unrenamed, and, like the economy, was largely unreformed. Across the street from the KGB building, in a pleasant little park, stood a bust of a Belarusian native son, founder of the KGB, Felix Dzerzhinsky. While the statue of the reviled Dzerzhinsky was allowed to be taken down after the end of the Soviet Union even in Russia, it remained standing in Belarus. Political repression, media censorship, and even accusations of state-sponsored “disappearances” continued, especially after the election of President Lukashenka in 1994. Likewise, the economic and industrial structure remained largely intact, and the elites of these sectors in power.

While moderately reformist forces, in the form of the Belarusian National Front and Shushkevich, struggled for power in the early days of independence, the conservative coalitions of the communists, *apparatchiki*, and industrialists managed to frustrate their efforts. This battle wore on between 1991 and 1994, when Shushkevich was ousted. The conservatives consolidated power in the presidency of Lukashenka, strengthening that office and finally allowing parliamentary elections to replace the conservative Soviet-era

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<sup>9</sup> Ministry of Statistics and Analysis of the Republic of Belarus, *Naselenie Respubliki Belarus'* (Minsk, 1996), p. 21.

<sup>10</sup> *Ibid.*, p. 22.

legislature. Not surprisingly given the questionable nature of the elections, the new legislature was also conservative, pro-presidential, pro-Moscow and anti-reform.

### *The independence movement*

The fact that nearly a decade after independence the Belarusian state remained largely authoritarian and the economy largely socialist does not mean that there were not segments of society pushing for democracy and reform. The Belarusian Popular Front (BPF) was perhaps the most important of these. Several events contributed to the birth of the BPF in 1988. The full effects of the explosion of the Chernobyl nuclear power plant in Ukraine two years earlier were only just coming to light after a perceived cover-up by Moscow. The nuclear material from the explosion of the reactor, located just south of the Belarusian border, had blown north, peppering the territory of tiny Belarus with fully 70% of the Chernobyl fallout. Secondly, the discovery of the NKVD killing field at Kurapaty provided some of the first evidence of Stalinist massacres. Lastly, Gorbachev's policy of glasnost had opened the door to discussion and dissent on such issues, as well as to the formation of new political groups in the neighboring Baltic republics of the Soviet Union.

The BPF was the first popular front formed in the Soviet Union outside of the Baltic states, and joined in allegiance with the Popular Front of Lithuania shortly after its inception. The BPF built its platform on national revival, independence, democracy, human rights, and restitution for the Chernobyl disaster. Mass pro-BPF, anti-Soviet protests took place in Minsk, but were met with violence by the Belarusian police.

Repression was such that, in 1989, the BPF held its first convention not in Belarus but in neighboring Lithuania.

In an attempt to preempt the threat posed by the BPF, the incumbent Communists structured the 1990 Supreme Soviet elections in favor of the Communist Party. Among other measures, 50 of the 360 seats were set aside for veterans' and other notoriously conservative groups. In the end, the BPF received only 26 of the 360 seats. In late July 1990, Belarus followed the lead of other Soviet republics in issuing a declaration of sovereignty. While this legislature did approve a sovereignty declaration, promoted tirelessly by the BPF, in July 1990, it did so with an eye to the preservation of ties with Moscow and the socialist economy through the Union Treaty. The declaration was not carried out in practice, however. Popular discontent grew within Belarus. Price increases, ordered by Moscow, precipitated the worst public demonstrations to date in Belarus. In April 1991, over 100,000 workers went on strike. The strikers were eventually assuaged, however, with promises of wage increases by the government of Prime Minister Kebich.

The Communist Party of Belarus and leaders in the government backed the conservative coup against Gorbachev in August 1991. After the coup failed, the Communist Party of Belarus broke from the Communist Party of the Soviet Union, hoping to avoid disbandment. The parliament declared its full support for independence on August 25<sup>th</sup>, in an attempted compromise with the BPF. The Communist Prime

Minister Kebich, who was closely allied with industrial interests,<sup>11</sup> and his cadres, who had supported the Soviet hard-liners in August, remained in power until 1994, and the same conservative Supreme Council, elected during Soviet rule, reigned until 1995. While the Communist Party of Belarus was suspended after the failed coup, it soon reformed into the Party of Communists of Belarus in 1992. Only the parliamentary chairman suffered ill consequences for his support of the August coup. The role of fall guy was imposed on the chairman of the Supreme Soviet, Nicholai Dememtei, who was forced to resign in September 1991 and was replaced by Stanislau Shushkevich, a rare political centrist on the Supreme Council.

Shushkevich came to be the strongest voice for Belarusian national independence and for political and economic reform. Shushkevich, however, faced a conservative, left-wing parliament and government (both backed by strong industrial interests) who constrained his ability to successfully implement such reforms. Shushkevich also faced opposition from the officer corps and the Ministry of Defense, which were predominantly ethnically Russian, and those with economic interests in the substantial military-industrial complex.<sup>12</sup> In early December of that year, Belarus hosted the meeting at which it, Russia and Ukraine agreed to dissolve the Soviet Union and establish the Commonwealth of Independent States. Shushkevich was also the force behind the CIS founding agreement with Yeltsin and Kravchuk to dissolve the Soviet Union, giving these states, finally, *de*

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<sup>11</sup> Dr. Nina Antonovich "Belarus: A Divided Country" (unpublished manuscript), Belarusian State University, Minsk, Belarus, 1999, p.6.

<sup>12</sup> Karen Dawisha and Bruce Parrott, *Democratic Changes and Authoritarian Reactions in Russia, Ukraine, Belarus and Moldova* (New York: Cambridge University Press, 1997), p. 248.

*facto* sovereignty. The CIS agreement, from the points of view of Shushkevich and Kravchuk, was a means to independence from Russia.

Shushkevich, who drew his strongest support from the “Westernized” agricultural regions of Grodna and from the reformers and intellectuals in the capital city of Minsk, was a free-market nationalist, and pushed for economic reform and a political and economic distancing from Moscow. Shushkevich’s efforts were largely frustrated by the conservative, leftist, Soviet-era legislature, however. In 1992, conflict intensified between the dominant left and the anticommunist opposition. The opposition launched a campaign calling for early elections to replace the legislature elected in 1990, but was defeated by the ruling Communist establishment. The Supreme Soviet lifted the ban on the Communist Party in February of 1993. Meanwhile, Shushkevich remained embattled against Vyacheslav Kebich, chairman of the Council of Ministers, who was anti-economic reform, pro-Moscow Communist, and backed by the industrialists. Kebich appointed a Supreme Council member by the name of Aleksandr Lukashenka to head a commission to investigate state corruption, specifically, corruption by Shushkevich. Despite Lukashenka’s open conspiring with conservatives Khasbulatov and Rutskoi in their failed attempt to wrest power from Yeltsin in Moscow, Kebich continued to support him and ignored BPF calls for his removal. In December 1993, Kebich and Lukashenka succeeded; Lukashenka denounced Shushkevich as corrupt. In January 1994, the conservative legislature approved a measure censuring Shushkevich for corruption. Shushkevich resigned and was succeeded by Mechislau Grib, a pro-Moscow, anti-market reform Communist ally of Prime Minister Kebich.

The first popular elections in Belarus did not take place until 1994. First round elections for the newly-created office of president took place in June. Aleksandr Lukashenka was seen as even more pro-Moscow and pro-status quo than Kebich or Grib. Lukashenka secured over 44% of the vote in first-round balloting, and won the run-off election by nearly six to one. Lukashenka was a historian by training, but a Communist Party official and agricultural manager by profession. Prior to his election, he managed various collective and state farms and served the Communist Party in positions on the farms, ranging from Commander for Political Education to Party Secretary.<sup>13</sup> From 1975 to 1977, he was also a political instructor for KGB border troops. He was a member of parliament at the time of the dissolution of the Soviet Union, which he opposed. He was thereafter a strong advocate of pan-Slavic unity and reunification. His popularity was enhanced by his strongly populist, anti-corruption image.<sup>14</sup>

It may at first blush seem that Lukashenka, given his background as a collective farm manager, should have appealed most strongly to agricultural constituencies. However, because of his pro-Moscow, pro-socialist and pro-industrial stands, he developed strong support in the heavily industry sector. Lukashenko ran to the left of Kebich, promising to reimpose fixed prices, reverse economic reforms carried out under the Kebich government, and reintegrate the Belarusian economy with Russia's.<sup>15</sup> In fact, in the first round of presidential balloting in June 1994, Lukashenka did best in the heavily-industrialized and Russified eastern and northern regions (in some of these places

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<sup>13</sup> "Elections in Belarus" [www.agora.stm.it/elections](http://www.agora.stm.it/elections), p. 1.

<sup>14</sup> "Summary of Belarusian Politics", [www.jura.uin-sb.de/law\\_pol/](http://www.jura.uin-sb.de/law_pol/), p. 4.

garnering half the vote in a field of six candidates). Lukashenka received his highest level of support -- 63% -- in the eastern industrial region of Magilyov. His promotion of a pan-Slavic national identity for Belarus may also have helped him win over Russian residents there. He did less well in the more agricultural, Catholic and Polish regions, receiving only 35% in the western Grodna province. His support was weakest in Minsk, where urban intellectuals and reformers still strongly backed the doomed Shushkevich.<sup>16</sup> While Lukashenka received 44% in the Minsk region as a whole, he received barely more than one quarter of the vote in the capital itself.<sup>17</sup>

Lukashenka, facing Kebich in the run-off election in July, received between 70% and 88% of ballots in each region, again doing best in industrialized areas and worst in western agricultural regions and the city of Minsk itself. It was in this second round of voting that Lukashenko's appeal to collective farmers helped. Those agricultural regions which had voted heavily for third candidates in the first round came to Lukashenko in the run-off election. In fact, Kebich lost ground in the run-off election (garnering *fewer* votes in a field of two than he had previously in a field of six) except in the Western, more Catholic and more Polish Grodna region, where he gained two percentage points. This swing vote from the "Westernizers" indicates the perception that Lukashenko was even further to the left, and a greater Russophile, than was Kebich.<sup>18</sup>

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<sup>15</sup> Karen Dawisha and Bruce Parrott, *Democratic Changes and Authoritarian Reactions in Russia, Ukraine, Belarus and Moldova* (New York: Cambridge University Press, 1997), p. 253-4.

<sup>16</sup> *Svaboda*, June 28, 1994, No. 25, p. 1.

<sup>17</sup> *Ibid.*, p. 3.

<sup>18</sup> *Svaboda*, July 1991, No. 27, p. 1.

*Consolidation of power by the left-wing conservatives*

The president's powers were further expanded after the election of Lukashenka. Lukashenka worked toward consolidation of power and repression of political dissent. He undermined the power of elected local councils by eliminating village and some town councils in October 1994. In November of that year, Lukashenka decreed himself the authority to appoint and dismiss local government officials and delegated to his local appointees nearly all local power. In May 1995, at the time of the first round of parliamentary voting, Belarusians were asked to vote on four referenda: to give the Russian language equal status with Byelorussian<sup>19</sup>; to create a state flag and seal based on that of the Soviet era; to promote economic integration with Russia; and, importantly, to give the president the right to dissolve parliament. BPF members protested the president's proposed referenda, refused to vote to approve it in the Supreme Soviet, and staged a hunger strike. Members of the president's security forces (which by this time were twice the size of the armed forces) beat the deputies on the steps of parliament. The remaining deputies promptly approved Lukashenka's referenda. All four referenda succeeded at the ballot.<sup>20</sup>

However, the fairness of the referenda and parliamentary elections held in 1995-1996 was, according to international observers, quite questionable. International observers found the elections to be neither free nor fair.<sup>21</sup> Lukashenka sought to ensure that the parliamentary elections and referenda would yield the desired outcomes. Making

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<sup>19</sup> Lukashenka advocated linguistic equality, and even superiority, of Russian over Byelorussian, and cultural as well as economic reunification of the peoples.

<sup>20</sup> "Summary of Belarusian Politics 1986-1996" [www.jura.uni-sb.de/~serko/law\\_pol/](http://www.jura.uni-sb.de/~serko/law_pol/), p. 5.

full use of state control of the media, he refused opposition candidates the opportunity to publicize their platforms, parties, and very existence. Liberal editors were dismissed. Programs linking the BFP to Nazi collaborators were aired on state television stations. The disbursement of government funds for elections was delayed, and limited to \$50 per candidate. The opposition was not the only target of Lukashenka's wrath, however. Lukashenka targeted the legislature per se in an effort to promote the pro-presidential referenda. Editorials came out against parliamentarianism itself as well as against the current Supreme Council.<sup>22</sup>

Belarus was the last state in Eastern Europe and the Newly Independent States to replace its Soviet-era legislature. Despite calls for early elections, the Communist-dominated, Soviet-era legislature served its full 5-year term. The results of the 1995 vote were just as the conservatives had hoped: a disaster for the BPF and for parliament in general. After the first round of balloting in May 1995, only 119 of the 260 seats were filled, far less than constitutionally required for quorum. The results were blamed on low voter turn out and on Lukashenka's publicly invalidating his own ballot as a sign of protest. The standing legislature repeatedly refused to hand over authority to the new delegates, despite the fact that their mandate had expired in March. After months of voting, finally, in November, 198 seats were filled and power was transferred to the new parliament.<sup>23</sup>

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<sup>21</sup> Karen Dawisha and Bruce Parrott, *Democratic Changes and Authoritarian Reactions in Russia, Ukraine, Belarus and Moldova* (New York: Cambridge University Press, 1997), p. 264.

<sup>22</sup> Karen Dawisha and Bruce Parrott, *Democratic Changes and Authoritarian Reactions in Russia, Ukraine, Belarus and Moldova* (New York: Cambridge University Press, 1997), p. 263.

<sup>23</sup> "Law and Politics in Belarus" [www.jura.uni-sb.de/~serko/law\\_pol/](http://www.jura.uni-sb.de/~serko/law_pol/), p. 1.

The conservatives' propaganda campaign had taken its toll: while the Belarusian Popular Front had fielded the largest number of candidates of any party, it failed to gain a single seat. Not a single member of the BPF was elected to the Supreme Council, and two of its most prominent leaders were subsequently driven into exile.<sup>24</sup> Few democratic opposition groups secured any representation in the May balloting. Instead, allied conservative communist and agrarian parties swept the elections. The new legislature was dominated by the pro-presidential Zhoda (Consensus) party, the Communist Party, the Agrarian Party, and the Civil Action Party, a social democratic party led by former national bank chairman Stanislau Bahdankievic.<sup>25</sup> The Party of Communists of Belarus, the largest faction, favored Belarusian-Russian reunification and the full restoration of the Soviet Union. While the Agrarians, the second largest group, differed from the Communists in favoring sovereignty for Belarus, they shared the Communists' stance on social and economic issues.

After the electoral victories of left-wing conservatives in 1994 and 1995, Lukashenka pursued further expansion of the powers of the presidency. In response to conflicts with the Constitutional Court and opponents in parliament over accusations that Lukashenka was attempting to rule by decree, in mid-1996 Lukashenka proposed massive revisions to the constitution. Prime Minister Chygir, whom Lukashenka had appointed after his election in 1994, resigned over the proposal. However, Lukashenka put the question to a referendum, and in November 1996 a new constitution strengthening the

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<sup>24</sup> Karen Dawisha and Bruce Parrott, *Democratic Changes and Authoritarian Reactions in Russia, Ukraine, Belarus and Moldova* (New York: Cambridge University Press, 1997), p. 244.

<sup>25</sup> "Summary of Belarusian Politics 1986-1996" [www.jura.uni-sb.de/~serko/law\\_pol/](http://www.jura.uni-sb.de/~serko/law_pol/), p. 6.

power of the presidency and extending Lukashenka's current term from 5 to 7 years was approved. The new law also gave Lukashenka further power over local governments, the ability to set election dates, appoint judges, including five of the eleven members of the Constitutional Court, and to appoint the officials of the Central Election Commission. The referendum also reformed the weakened legislature into a bicameral assembly consisting of an 110-member House of Representatives and a 64-member Council of the Republic.

Skepticism regarding the 1996 balloting was widespread, both at home and abroad. Prior to the balloting, the Constitutional Court ruled that the vote was not binding and opposition legislators initiated impeachment proceedings against Lukashenka. 10,000 protestors reportedly marched in protest against the president prior to the vote, eliciting a government crackdown on political expression and public rallies. Even after the election, many legislators questioned the legitimacy of the new structure of parliament, and 40 refused to participate. Officially, 70% of voters favored the new constitution. Many international observers questioned the legitimacy of the elections, however. The government's tactics spurred criticism by the Council of Europe, the EU Council of Ministers, and others. Despite this, the government continued its policies. Arrests and media control continued. Lukashenka appointed sympathetic judges to replace those members of the Constitutional Court who had resigned in protest after the 1996 balloting, and managed to find enough loyalist conservatives in parliament to transfer authority to the restructured legislature.

#### **IV. Policy: Embracing Dependence and Russian Reintegration**

##### *Foreign policy*

Shushkevich pursued a policy of neutrality, even in the face of substantial opposition. Both Shushkevich and Ukraine's Kravchuk refused to sign the collective security agreement proposed by Russia at Tashkent in 1992, asserting that it would violate their states' policies of neutrality and military nonalignment. Shushkevich faced resistance to this policy not only from abroad, that is, from Russia, but also from within. This argument was later denounced by the more conservative parliament. Two months after Tashkent, the conservative Prime Minister Kebich signed an agreement with Russian Prime Minister Yegor Gaidar on a common economic, political and social space between Russia and Belarus.<sup>26</sup> In 1993, Prime Minister Kebich put a collective security pact before the Supreme Council, proposing an economic and defense union with Russia. The Supreme Council approved the pact, much to Shushkevich's chagrin.

The conservative Supreme Council hesitated regarding full integration, hoping that Yeltsin would soon pass from the scene and that a less reform-minded union might be established. To this end, many Belarusian luminaries, including then-Supreme Soviet member Lukashenka, aligned with anti-Yeltsin forces in Russia led by parliamentary speaker Ruslan Khasbulatov and Vice President Aleksandr Rutskoi. Yeltsin's victory over Khasbulatov and Rutskoi in the standoff at the Russian White House in October 1993 led to BFP to call for the removal of deputy Lukashenka and three of his allies.

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<sup>26</sup> Karen Dawisha and Bruce Parrott, *Democratic Changes and Authoritarian Reactions in Russia, Ukraine, Belarus and Moldova* (New York: Cambridge University Press, 1997), p. 248.

Instead, Kebich continued to support Lukashenka and used him to force out Shushkevich, as previously outlined.

Under the Shushkevich government, the foreign policy of Belarus struck a balance between accommodation with Russia and accommodation with the West, reflecting the struggle between the pro-reform, anti-Moscow president and the conservative legislature. On the one hand, the Belarusian foreign minister laid claim to portions of Lithuania that had been under Polish rule during the interwar period. Belarus hosted and was party to the founding talks of the CIS, and promised to serve as the capital of that international organization thereafter. On the other hand, Belarus agreed to surrender its stock of nuclear weapons to Moscow in exchange for \$59-million US government pledge to assist in the dismantling of the stockpile.

After the victory of the conservatives under Lukashenka, Belarus moved closer toward political and economic reunification with Russia and into further isolation from the West, a goal that contrasts sharply with the globalizer strategies. While Belarus joined NATO's Partnership for Peace program in January 1995, by 1999 it had still not agreed on the requirements of its actual participation. Lukashenka became a vocal opponent of NATO expansion. A month later, out of frustration with the lack of progress on reintegration in the multilateral context of the CIS, Belarus signed a bilateral treaty with Russia. The agreement provided for joint border protection and the eventual establishment of a body to govern a joint economic and monetary union. In April 1996, Belarus and Russia signed the Treaty on the Formation of the Community of Sovereign Republics, which laid the groundwork not only for economic union, but political and

military union as well. Russian Prime Minister and former natural gas *apparatchik* Victor Chernomyrdin was appointed the first head of the CSR executive committee that August.

The preamble to the Union Treaty states that Russia and Belarus seek a "deeply politically and economically integrated community" based on "the idea that the two nations have historically common faiths".<sup>27</sup> Progress on implementation of the CSR treaty remained slow, in large part because of reservations on Russia's part regarding the cost of the union. However, in May 1997, Presidents Yeltsin and Lukashenka signed a revised and more detailed Charter of the Union. The two also formulated a budget and agreed to spend \$10.2 million in 1998 on reintegration. The Charter was ratified by the legislatures of both states and came into effect in June 1997.<sup>28</sup>

### *Economic policy*

Under the Kebich government, reintegration with Russia was seen as the alternative to market reforms as a means to sustain the economy. Soviet economic, ministerial and planning institutions (with the exception of the much-reduced military) remained largely intact. While Shushkevich pushed for economic reforms, most of these reforms were effectively blocked by the left-wing coalitions in the government and legislature. The majority of those market-oriented measures that did pass were soon reversed by the Lukashenka administration.

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<sup>27</sup> *Treaty on the Formation of a Community Between Belarus and Russia*, Administration of the President of Belarus Home Page, [www.belarus.net](http://www.belarus.net), p. 1.

Economic policy under the Lukashenka government was also decidedly anti-market. Beginning in 1995, Lukashenka launched a campaign of renationalization of many of the small number of concerns that had been privatized. Strict controls were placed on access to foreign currency. Many firms were placed under the direct control of members of the government and executive. Such firms generally enjoyed substantial tax breaks, largely avoiding corporate taxes, which could reach as high as 70%. Some firms, under the direct control of the president, were exempt from taxes altogether.

Belarus' late economic growth in 1997 under Lukashenka was fueled by an enormous expansion of credit and the printing of rubles. As a consequence, inflation increased as well, just as the exchange rate (official and unofficial) plummeted. High inflation also provided the illusion of profitability to enterprises, which would otherwise be making a loss. Unsold inventories continued to mount. Russia's agreement to accept 70% of energy payments in barter helped to fuel production. However, Russian suppliers often had difficulty finding Belarusian products they wished to purchase, as they had no say over the structure or quality of production.<sup>29</sup>

Privatization was suspended. Industrial credits were extended. Price controls were reinstated and taxes on the small private sector prohibitively high. Inefficiency in production remained high, with virtually all sectors (construction, industry, agriculture) more efficient in neighboring countries like Poland (making imports cheaper than domestic production, had Belarus engaged in open trade). Official Belarusian statistics

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<sup>28</sup> "Belarusian parliament ratifies Union Treaty -- Lukashenka favors restoration" NUPI Centre for Russian Studies Database, [www.nupi.no/cgi-win/Russland/personer.exe](http://www.nupi.no/cgi-win/Russland/personer.exe), p.1.

put loss-making enterprises at 15%. Independent estimates place the figure at closer to 70%. Lukashenka nationalized the Interbank currency exchange, subordinated the formerly-independent Belarusian Chamber of Commerce, nationalized large, highly-visible enterprises such as the Hotel Planeta and Dyuna Company, and liquidated the Antimonopoly Ministry, which obviously conflicted with his economic policy. Not surprisingly, Belarus had one of the lowest levels of foreign direct investment in the NIS.<sup>30</sup>

Belarusian President Lukashenka sought a "special relationship" with Russia, hoping that reunification with Russia would lighten Belarus' debt burden as well as give Belarus energy at the lower Russian domestic price. Lukashenka and his industrialist comrades benefited from Russia's discounted gas shipments, and united with pro-Russian groups to push reunification and reintegration with Russia. The Belarusian economy was expected to grow in the short term only as a result of further industrial "soft credits" (subsidies) from the state.<sup>31</sup> Medium-term economic prospects were even less rosy, as inflation was expected to rise still further. Market reforms have not proceeded in Belarus as they have in many other post-Soviet states, and the economy was still largely based on credits from the government, which were in turn subsidized by cheap energy from Russia. Russia continues to be by far Belarus' most important trading partner, and the volume of Russian-Belarusian trade continues to grow. Russia accounts for approximately half of

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<sup>29</sup> Dr. Stanislav Bogdanovich and Jaroslav Romanchuk, "Economic and Social Policy of the Republic of Belarus" (unpublished manuscript), Belarusian State University, Minsk, Belarus, April 1991, pp. 3-5.

<sup>30</sup> Dr. Stanislav Bogdanovich and Jaroslav Romanchuk, "Economic and Social Policy of the Republic of Belarus" (unpublished manuscript), Belarusian State University, Minsk, Belarus, April 1991, pp. 3-7.

Belarus' imports and exports, with Ukraine a distant second at 13-14%. Trade with Western countries remains relatively small.

### *Energy policy*

Like many countries of the former Soviet Union, Belarus was a prisoner of the pipeline. Natural gas and oil were cheap and plentiful in the Soviet era, and were supplied directly to the republics through an elaborate web of pipelines from Russia and the East. Conservative coalitions chose to embrace this dependence rather than reform or reorient the economy. While some increases in efficiency were realized in industrial gas consumption and energy consumption overall (Chapter 3), these gains were relatively modest by post-Communist standards. At the same time, industrial consumption of oil actually increased since 1992, and net imports as a share of consumption in 1997 were still 89%, compared with 91% in 1992, virtually unchanged since independence. Belarus remained highly dependent on energy imports, and almost exclusively on imports from Russia.

Belarus continued to import virtually all of its natural gas and oil – the most important energy imports – from Russia. In 1997, 99% of crude oil and 100% of natural gas were imported from Russia. Even in imports of processed petroleum products (a relatively minor category by quantity and value), Belarus imported 90% (by volume) from Russia. Belarus continued to enjoy preferential prices (both compared to CIS and non-CIS importers) as well: the average price of petroleum products imports from Russia in

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<sup>31</sup> EIU *Country Report: Belarus*, 3rd Quarter 1997, p. 3.

1997 was US\$176 per metric ton, compared with an average price from non-CIS exporters of US\$287 per metric ton. Russia's natural gas export price to Belarus in 1996 was US\$50.3 per thousand cubic meters, compared with US\$75.2 per thousand cubic meters to non-CIS countries. Belarus managed to maintain Russian subsidies in crude oil as well: Russian prices in 1997 to Belarus were US\$107 per metric ton compared with \$119 for non-CIS states. In 1996, Belarus' price was US\$95 per metric ton, compared to US\$133 for non-CIS states.

Table 6.1 Crude Oil Imports to Belarus, 1995-1997 (value in thousands of US dollars)

	1995	1996	1997
from Russia	895116	1013389	1119684
as % of total	99%	100%	99%
Total	902915	1013389	1122797

Source: *External Economic Activities of the CIS Countries* (Moscow, Russia: Interstate Statistical Committee of the CIS, 1999, 1996, 1995).

Table 6.2 Natural Gas Imports to Belarus, all from Russia, 1992-1997 (billions cubic meters)

1992	1993	1994	1995	1996	1997
18	16.2	14.3	13.5	13.7	16.2

Source: *External Economic Activities of the CIS Countries* (Moscow, Russia: Interstate Statistical Committee of the CIS, 1999, 1996, 1995) and *Statisticheskii Biulleten', Iunya 1996*, Nomer 11, pp. 130. Mezghosudarstvennyi Statisticheskii Komitet Sodrzhestva Nezavisimyykh Gosudarstv, Moskva, Rossiia (Commonwealth of Independent States).

Table 6.3 Imports of Petroleum Products to Belarus by Exporter, 1996-1997 (value in thousands of US dollars)

	1996	price per ton	1997	price per ton
Russia	69622	\$175	124494	\$176
CIS	72727	\$179	126473	\$178
non-CIS	17857	\$319	20381	\$287
Total	90584	\$196	146854	\$188

Source: *External Economic Activities of the CIS Countries* (Moscow, Russia: Interstate Statistical Committee of the CIS, 1999), pp123-124.

For Belarus, only coal was more cheaply bought from non-CIS countries. Crude oil, oil products, gasoline, and diesel were all available less expensively from the CIS. Belarus imported fuel oil and natural gas exclusively from the CIS.

Table 6.4 Average Import Prices of Energy Products to Belarus, 1995-96

	1995		First Quarter of 1996	
	from CIS	from non-CIS	from CIS	from non-CIS
Coal	45	22	45	29
Crude Oil	79	119	91	-
Processed oil products (pererabotiki)	169	326	169	313
Gasoline	203	212	250	351
Diesel Fuel	170	202	154	...
Fuel Oil	70	-	110	...
Natural Gas	53	-	50	-

Source: *Statisticheskii Biulleten'*, Avgust 1996, Nomer 16, pp. 101, Mezghosudarstvennyi Statisticheskii Komitet Sodruzhestva Nezavisimykh Gosudarstv, Moskva, Rossiia (Commonwealth of Independent States). Units in US\$ per thousand cubic meters for natural gas and in US\$ per metric tonne for all others.

Export pipelines from Russia to Western Europe ran under both Ukraine and Belarus. However, disputes regarding shipment volumes and fees with one made deals with the other more attractive. Russia decided to favor Belarus and concentrated new energy transit projects there. While Russia's other export routes traveled through hybrids such as Lithuania and Ukraine, which were actively seeking fuel supply diversification through construction of oil import terminals at Buting and Odessa, respectively, Belarus remained a reliable transit partner. Russia sold fuel to Belarus in reliable quantities and at low prices, while Belarus reliably delivered the through-put and levied low transit fees.

While Belarus decreased energy consumption somewhat, it did not switch to alternative fuel exporters. In the first three-quarters of 1995, for example, Belarus imported \$1,349,000,000 in mineral products (the major component of which is fuel products) from the CIS, nearly 32 times the volume of mineral products imports from other countries. These imports totaled 42% of Belarus' total imports and 59% of its imports for the CIS.<sup>32</sup> Clearly, Russia remained Belarus' main source of energy.

Belarus remained almost entirely dependent on Russia for its energy, both gas and oil. It was in arrears for both commodities to Russia. The debate over the exact size of the debt has grown vitriolic at times, causing the Russian gas company, Gazprom, to occasionally threaten to cut off Belarus. Russia temporarily suspended deliveries of oil and gas in August 1993 and again in September 1994 for nonpayments. Russia used this second instance as an opportunity to negotiate for ownership of the Belarusian gas company in lieu of payments. To Russia's chagrin, the Supreme Soviet of Belarus refused to ratify the agreement. Belarus began allocating energy to "priority sectors" to reduce consumption, and finally agreed to a payback schedule when Russia threatened to re-route energy exports to Europe through Latvia or Lithuania instead of through Belarus. Nonetheless, Belarus had difficulty meeting this schedule.

In 1995, after the election of Lukashenka, Russia became less demanding in its payments. The two countries agreed that Russia would supply Belarus at lower-than-

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<sup>32</sup> *Statisticheskii Biulleten'*, Mart 1996, Nomer 5, pp. 38, *Mezhhgosudarstvennyi Statisticheskii Komitet Sodruzhestva Nezavisimykh Gosudarstv, Moskva, Rossiia* (Commonwealth of Independent States)

market prices in exchange Belarusian exports, a barter agreement favorable to Belarus.<sup>33</sup> Russia again reduced supply in July 1997 for a few days, spurring Belarus to promise to a more demanding repayment schedule, through both cash and barter.<sup>34</sup> It remained to be seen if Belarus would abide by this agreement more closely than the numerous past agreements.

The fact of continued Russian energy deliveries despite nonpayments in effect constitutes a subsidy of the Belarusian state and economy. Furthermore, Belarus hoped that economic reintegration with Russia would lead Russia to forgive some of its energy debt and provide it sustained access to these subsidies. These arrears are in part due to the failure of industrial and domestic consumers to pay the state-run Belarusian gas distribution company, Beltransgaz. Other state-owned industries have been ordered to increase production, which is to be used as barter to pay off the debt to Russia. Meanwhile, the state had issued low-interest loans to both selected public and private consumers to help them "pay" their gas debt to the government, which is expected to only increase inflationary trends.<sup>35</sup>

The questions of Belarusian-Russian integration and of energy trade are inextricably interlinked. Gazprom, though it has occasionally put the screws to Belarus, has in general been very lenient regarding the matter of Belarus' debt, particularly after 1994. Gazprom is willing to pay this price in exchange for secure access routes to Western markets; Gazprom Chairman Vyakhirev publicly praised Lukashenka as the

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<sup>33</sup> Library of Congress, *Belarus and Moldova: Country Studies*, 1995.

<sup>34</sup> EIU *Country Report: Belarus*, 3rd Quarter 1997, p 14.

<sup>35</sup> Ibid.

"leading integrator in the CIS". Shortly after the Union Treaty was signed, Gazprom began construction on the Yamal-Hamburg pipeline that would carry 68 billion cubic meters of gas from Siberia to lucrative Western European markets, through Belarus, ensuring supply for some time to come.<sup>36</sup>

## **V. Conclusion**

The early period of independence in Belarus was characterized by political dissent and contention between a moderate pro-independence and pro-West coalition of reformers, backed by "Westernized" agricultural regions and urban elites in the capital, and pro-Russian, anti-reform coalitions backed by industrial and military interests. The reformers, represented by the Belarusian Popular Front and Shushkevich, were never able to fully wrest power from the conservatives, who fought to preserve the obstructionist Soviet-era legislature and to recapture the weak executive branch. After the ouster of Shushkevich, the conservatives further consolidated power as the presidency passed to Lukashenka, by strengthening the now conservative-dominated executive branch and by ensuring the election of a conservative left-wing pro-presidential legislature. This domination by conservative coalitions ensured pro-industrial, pro-Moscow policies and Belarus' status as a Russophile.

Belarus sits squarely in the east, not only in terms of energy trade, but increasingly in terms of aid as well. Bilateral aid from Western European countries has dried up, and even the World Bank has moved its Belarus operations to Ukraine. Russia remains

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<sup>36</sup> "Gazprom praises Belarus as 'leading integrator in the CIS'. NUPI Centre for Russian Studies

generous, however, and has promised to loan Belarus 500 billion rubles for increased industrial production.<sup>37</sup> Still, the greatest danger to the Russophile model may be Russia itself. While the Belarusian leadership refused to engage in marketization and rationalization of the economy, these processes may indeed take shape in Russia. Should Russian foreign policy goals change, should it find more lucrative export corridors for its fuel to Western Europe, should it encounter a deep economic crisis, Russian leaders may decide the energy subsidies (pricing structure, barter agreements, credits) which keep the Belarusian economy afloat are simply too much to bear. It is unclear how Belarus could maintain its industrial and agricultural base, indeed its very economy, without them.

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Database, [www.nupi.no/cgi-win/Rusland/krono.exe](http://www.nupi.no/cgi-win/Rusland/krono.exe), p. 1.

<sup>37</sup> EIU *Country Report: Belarus*, 3rd Quarter 1997, p 15.

## **CHAPTER VII**

### **CONCLUSION: “TRANSITIONS” & UNEVEN GLOBALIZATION**

#### **I. State and Society in “Transitology”**

The study of post-socialist transitions can be separated generally into two camps: those who support the implementation of rapid economic reform, variously known as “shock therapists,” “neo-liberals,” or “market reformers,” and those who advocate a more gradual, state-led approach to economic restructuring, known as “gradualists” or “evolutionary theorists.” While much of value can be learned from both camps, I will argue that our understanding of economic transition could be enhanced by drawing on the fields of international political economy and the state-in-society approach. Indeed, some transitologists have begun to draw on ideas from these other fields, with (I will argue) interesting and important results. This study has sought to expand this line of inquiry still further.

The first school of students (and in some cases practitioners) of transition argues that the most successful economic reforms have resulted from sudden and wide-ranging economic reforms. Such “shock therapy,” supported by neo-liberals such as Brada, Aslund and Hellmann, they argue, promotes the most complete and unencumbered transitions to capitalism. Rapid market liberalization, particularly accompanied by quick and large-scale privatization, promote the responsiveness of firms to market signals, building the foundation of a market-based economy. Furthermore, rapid liberalization and wide-ranging reform help to bypass existing elites who might resist reform, thus

ensuring the continuation of that policy trajectory. These policies, say their advocates, help to combat spiraling inflation, create functioning markets, introduce private ownership and capitalist institutions, lay the foundation for future economic growth, and integrate these markets into the world economy. They also help to prevent “dysfunctional” economic behavior characteristic of countries in which Socialist-era institutions, enterprises and methods of management persist.<sup>1</sup>

The second, “evolutionary” school, supported by scholars such as Murrell, Stark, Poznanski and Woodruff, holds that such shock therapy has produced massive economic dislocation and economic decline. Instead, these theorists advocate a gradual approach to reform, allowing the institutions of the former regime to persist as new institutions, markets, and forms of ownership are introduced. Peter Murrell<sup>2</sup> argues that shock therapy failed in its goal of implementing top-down reforms which by-pass existing social and economic forces, and that an evolutionary approach is more likely to generate economic progress sustained over the long term. Instead, most of the economic success credited to shock therapy (specifically the case of Poland<sup>3</sup>) was in fact due to pre-existing institutions and social structures on which economic recovery could be built. The relative weakness of such structures in Russia ensured its continued decline, leading to accusations of too much “shock” and not enough “therapy.”

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<sup>1</sup> Josef Brada “The Transformation from Communism to Capitalism: How Far? How Fast?” *Post-Soviet Affairs* 1993, V. 9, No. 2, pp. 87-110.

<sup>2</sup> Peter Murrell “What is Shock Therapy? What Did it Do in Poland and Russia?” *Post-Soviet Affairs*, 1993, V. 9, No. 2, pp. 111-140.

<sup>3</sup> Kazimierz Poznanski, *Poland's Protracted Transition: Institutional Change and Economic Growth 1970-1994* (New York, N.Y.: Cambridge University Press, 1996), and Kazimierz Poznanski, ed., *The Evolutionary Transition to Capitalism* (Boulder, CO.: Westview Press, 1995).

A problem with both the shock therapists and gradualists is the assumption that state policy is, and should be, geared toward economic transition. The question for transitology is not if the transition to a market will take place, but rather how and when. Here transitology could again benefit from an insight of state-in-society analysis: such goals and priorities of the state should not be assumed. A lack of elite capacity cannot be the only explanation for slow progress toward transition: elites may find it in their interest to preserve the status quo, or to construct a hybrid economy with its multiple opportunities for rent-generation. The social forces allied with the state must be examined in order to understand the policies issuing therefrom. This questioning of state priorities opens the door to questioning the assumption of a linear developmental path to the possible sustainability and self-reinforcing nature of other outcomes, such as stable Russophile or hybrid systems.

A second area in which transitology might benefit from state-in-society analysis is in its examination of non-material modes of organization and mobilization. I have argued that the power of ideas, identity and ideology, in addition to material motivations, have causal significance. The “transition” process is one of reshaping not only economies and national institutions, but of reshaping nations themselves. The significance of such factors should not be underestimated. The process of transition should also be understood in the international and regional context within which individual states find themselves. The politics of post-socialist states do not exist in a vacuum. External incentives and constraints (energy dependence, for example) provide the opportunity

structures within which state leaders and social forces vie for power. These factors should be explicitly integrated into our model of transition.

There is a developing body of literature within the study of transition that seeks to incorporate insights from other fields of social science, and to explore the relevance of other explanatory variables. Stephen Hanson, in "Analyzing Post-Communist Economic Change,"<sup>4</sup> argues that both schools of transitologists, the shock-therapists and the gradualists, underestimate two essential factors in the success of economic transformation: constraints on policy-makers by interest groups and the structural position of the country in the international economy. All of the theorists' policy prescriptions, as disparate as they may be, depend essentially on elites' ability to transcend interest groups.<sup>5</sup> This, Hanson argues, may simply be impossible in some cases:

For elites in Russia, Ukraine, and not other newly independent states of the CIS, the predominance of nonviable enterprises, as well as the fact that land, labor and money markets are either poorly developed or entirely absent, combine to constrain politicians' choices even more severely. Under such circumstances, both shock therapy and state-led gradualism are politically unfeasible... Politicians facing these depressing options have generally chosen to muddle through with a hybrid strategy.<sup>6</sup>

Thus, the constraints on state action posed by social groups may drive the state necessarily to seek accommodation with social forces at the expense of an abstractly "optimal" strategy. This line of reasoning is essential to our understanding of state strategy, making state-society relations a cornerstone of our analysis of state strategy.

Hanson, in his article "Dependency, Development, and Devolution: The Anomalous Political Economy of Communist and Postcommunist Societies," also argues

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<sup>4</sup> Stephen Hanson, "Analyzing Post-Communist Economic Change: A Review Essay" *East European Politics and Societies* V. 12 No. 1, Winter 1998, pp 145-170.

<sup>5</sup> *Ibid.*, p. 167.

that both the literature of comparative political economy and that of transitology could benefit from an end to their mutual isolation. Hanson views the collapse of the Soviet Union and subsequent patterns of marketization through the lenses of modernization, world-systems and rational choice theories. While he finds insights in each, he also finds them individually wanting. No one is able to explain all post-Soviet outcomes, and none can identify “any mechanism by which new formal macroeconomic structures are created by organized individual actors.”<sup>7</sup> Hanson argues for a more comprehensive political economy paradigm, one which integrates “ideological modes of coordinating collective action” in addition to material ones. This study had attempted to do just that.

Hanson also argues that state strategy is only a single determinant – and perhaps a minor determinant – of transition outcomes. Geographical position and proximity to the European Union are better indicators of successful economic transition than shock therapy versus gradualist strategies, he argues in both articles. His argument holds for the general case: EU countries may find it economically advantageous and in their security interest to bolster and engage the economies on their immediate eastern borders. This specific targeting of investment and support may change the international opportunities facing some states. Furthermore, regional context is important: post-Soviet states located between Russia and China or Russian and the Middle East face different opportunities and constraints than do states situated between Russian and Western Europe.

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<sup>6</sup> Ibid., p. 169.

<sup>7</sup> Stephen Hanson “Dependency, Development, and Devolution: The Anomalous Political Economy of Communist and Postcommunist Societies,” in *Environment and Planning C: Government and Policy*, Vol. 16 No. 2, April 1998, 225-246.

This analysis is an essential step toward understanding the importance of international political economy to the possibilities for economic transition. The constraints and opportunities facing elites construct the environment within which ruling coalitions form and formulate policy. However, geography alone cannot explain the full range of transition outcomes (see Chapter I). Instead, physical location is only part of the story. Domestic institutional context, the nature of the state, state policy and consistency, and the orientation of society play as large a role in inducing (or discouraging) international investment and governmental alliances as does geographical proximity. Some of what might masquerade as external factors are in truth internal: some of the "advantages" enjoyed by the non-NIS in Central and Eastern Europe, such as a history of greater autonomy from Soviet rule, relative decentralization of planning, and escape from Stalinist collectivization of agriculture, are not a function of current proximity to the EU, but rather facets of domestic institutions and state-society relations. Is it the presence or absence of such aspects -- friendly structures, in addition to location -- which facilitate international investment, the merging of markets, and "transition" in Central Eastern Europe.

Some of these transitologists have begun to incorporate, implicitly or explicitly, the role of social actors and of state-society relations into their analysis. Valerie Bunce<sup>8</sup> sees the development of social groups with shared economic, political, social and cultural experiences, with common goals, identities and definitions of the enemy, and empowered by ideology, organization and leadership, as key to the nature and timing of socialist

collapse. The development and effectiveness of these groups, however, are determined by two important variables: the institutional context of the country's specific socialist past and the expansion of political opportunity structures that shift the costs and incentives for given social groups. Bunce's cases include the entire universe of post-socialist Europe, and the many forms of socialism encompassed there. Bunce introduces two key elements into the debate: social networks and movements and changes in the international context. Bunce's study addresses the causes of collapse, an ambitious task in itself. However, she does not seek to explain the evolution of politics thereafter, and (understandably, therefore) treats the Soviet Union as a single case rather than as fifteen separate cases. However, she explains difference in social groups in different countries entirely by differences in institutional context. This approach must be expanded in the post-Soviet cases in order to account for divergent outcomes in social groupings based in very similar institutional histories.

Davis Stark and Laszlo Bruszt<sup>9</sup> argue that in fact democratization strengthens economic transition and marketization. Contrary to liberals who argue for the freeing of markets and to "involutionists" who argue for the freeing of the state, Stark and Bruszt argue that extended accountability through deliberative associations and embeddedness in beneficial institutional constraints actually enhance the authority of the state to carry out reforms. The associative and discursive properties of the facilitating institutions help to simultaneously strengthen both markets and states. And yet it is not democratization *per*

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<sup>8</sup> Valerie Bunce *Subversive Institutions: The Design and the Destruction of Socialism and the State* (New York, N.Y.: Cambridge University Press, 1999).

<sup>9</sup> David Stark and Laszlo Bruszt *Postsocialist Pathways: Transforming Politics and Property in East Central Europe* (New York: Cambridge University Press, 1998).

se. that enhanced the state's formulation and implementation of a coherent reform strategy: for Stark and Bruszt, the "unfettered electoral competition"<sup>10</sup> in Hungary went hand-in-hand with the government's "lurching from one extreme policy current to another, each provoking a new round of crisis."<sup>11</sup> Instead, the defining characteristics of successful economic transformation are the nature of the social networks and their ties to the state. Stark and Bruszt focus their analysis on the states of Central Eastern Europe – some of the most sterling examples of transformative success in the post-socialist world. These are states which benefited from both proximity to the European Union and less onerous domestic institutional legacies, and were all extremely successful reformers. It would be interesting to extend their analysis to negative cases as well, to examine the differences in the predominant social organization in a fuller range of cases. One cannot talk only of state embeddedness and accountability to understand success or failure in transition, but embeddedness in what sort of institutions, and accountability to whom?

The legacy of Soviet institutional structures and state-society relations shaped the possibilities for reform, and helped to produce the new and self-reinforcing forms of economic structures. David Woodruff<sup>12</sup> argues that the emergence of Russian's pervasive barter system in the early 1990s was a reaction not to hyperinflation (as conventional wisdom would hold), but rather a product of social groups seeking to protect their power and interests and the local level. Woodruff employs a "sociological-institutional" approach to the problems of Russian monetary consolidation. He finds that, because the

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<sup>10</sup> Ibid., p. 8.

<sup>11</sup> Ibid., p. 11.

<sup>12</sup> David Woodruff *Money Unmade: Barter and the Fate of Russian Capitalism* (Ithaca, N.Y.: Cornell University Press, 1999).

rigid structures of Soviet production bound local authorities to in-kind taxation, and a consolidation of federal monetary authority would undermine local economies and the provision of critical services, local authorities and social networks turned to non-monetary exchange and the establishment of local currencies. Monetary consolidation, or the acquisition by the state “of a monopoly over the means of payment that is used across the territory it rules.” is an essential (if sometimes underestimated) facet of state-building,

Thus, the battles over currency between local and federal authorities were struggles not only over preservation of the local economy, but over sovereignty itself. Local and regional coalitions of state authorities, enterprises, and threatened workers constructed a system of alternative exchange that accounted for an estimated 50-70% of industrial sales. While a barter system is arguably less efficient than monetized markets because of increased transaction costs, it does serve to protect the power and livelihoods of those involved. It is another example of how social actors, allied with a stratum of the state, establish economic forms neither “socialist” nor “capitalist.”

Joel Hellmann helps to clarify the political reasons behind “partial reform” with his argument that the enemy of sustained reform is not necessarily the short-term loser as much as it is the short-term winners. Hellmann argues that, contrary to much of the current thinking, the gains of economic reform (particularly partial reform) are not necessarily dispersed throughout the economy. Like the costs, they can be concentrated in the hands of a relatively narrow segment of society:

Both comprehensive and partial economic reforms produce winners in the short term, with gains partly or wholly determined by rents generated by the existence of distortions in the developing market economy. Moreover, these rents are highly concentrated,

benefiting those in a position to arbitrage between the reformed and unreformed sectors of the economy.<sup>13</sup>

These short-term winners are actors who are in positions to collect rents generated by the market distortions inherent in partially-reformed economies, the arbitrage between the state-structured and free-market portions of the economy. These actors can include the former communist elite, bureaucrats, officials, heads of state farms or enterprises as well as new commercial bankers, fund managers, and some private entrepreneurs.<sup>14</sup> These “winners” have an incentive to preserve these market distortions and seek to influence the ongoing reform process. These groups and networks can help us to understand the resistance to full market reform in the hybrids in particular.

What is good for these “winners” is not necessarily what is good for the broader economy: Hellmann argues that partial reforms in general create greater income gaps and slower economic recoveries than in “advanced” reformers or those with the least reform. These findings are consistent with our conclusions regarding the hybrids versus the globalizers and Russophile.<sup>15</sup> Also consistent with our findings is the fact that the globalizers experience higher levels of unemployment than do the hybrids or Russophile. These pro-partial reform policy coalitions may indeed serve to prolong (perhaps indefinitely?) the period of painful market distortions of the hybrid economy. This form of economy itself begins to generate a self-perpetuating constituency.

However, Hellmann also argues that those states which are most politically accountable to the economic losers are also those most likely to sustain and advance

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<sup>13</sup> Joel Hellmann “Winners Take All: The Politics of Partial Reform in Postcommunist Transitions” *World Politics* 50 (January 1998), p. 220.

<sup>14</sup> *Ibid.*, p. 229.

economic reform. As evidence, he cites countries like Belarus as a politically unaccountable, and therefore economically unreformed, country. As positive cases, he cites states such as Estonia and Latvia as politically accountable and therefore economically reformed. While Hellmann's broad categories are certainly useful, closer examination of the specific cases is warranted. In assessing the political vulnerability of the regimes, too little weight is given to the exclusion from national voting of approximately one third of the population, the bulk of whom are some of the most ill-effected economic losers. Thus, I would argue, Estonia and Latvia are quite a bit less responsive to economic losers than Hellmann might assume. Secondly, I would argue that political insulation or lack of vulnerability in and of itself does not guarantee economic reform. In order to understand the goals and priorities of the state, one must first examine the interests and priorities of those social groups closely allied with the state, such as beneficiaries of the old economy or beneficiaries of Hellmann's partial reform. Thus, Belarus' status as a relatively politically invulnerable regime with a relatively unreformed socialist economy is not surprising, considering the government's strong ties to conservative forces such as heavy industrialists and state farm chairmen.

A second caveat with Hellmann's definition of political vulnerability is his operationalization of this variable as the number of political turnovers of government. It is essential as well to examine the nature and political spectrum of these governments: is the government turnover between radical reformers and hard-line conservatives, or

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<sup>15</sup> Ibid., p. 225.

between radical reformers and more moderate reformers? These questions directly impinge on the question of the consistency and advancement of reform.

## **II. Uneven Globalization: The NIS Face Their Future, and Their Past**

Hopefully this study has provided a closer look at the complexity of attitudes toward globalization among groups in emerging states. The received wisdom is that coalitions fall into a dichotomy regarding the process of globalization. Those which are “pro-globalization” are pro-free market, engaged in the more competitive sectors of the economy, and are internationalist without pretensions to particularistic identities. “Anti-globalization” coalitions are composed of the economic losers in the economy, those who favor statist models of economic management, and those with strong nationalist or confessional assertions of identity. In truth, the alignment of these issues among the coalitions is more complex. In this study, the ruling coalitions which were most strongly pro-globalist and pro-market were also those who were most virulently nationalist. In fact, they drew on that sense of nationalism to help ensure the success of the globalist agendas. Those ruling coalitions that were most strongly statist and anti-globalization often rejected nationalism outright.

The fact that politicians would co-opt nationalistic movements to secure support for their and their supporters’ economic goals is not the most surprising aspect of this study. Instead, it is the fact that globalists can also be nationalist and that statist may in some cases be the most ethnically tolerant must make us question the argument that the

resurgence of nationalism around the globe is necessarily a reaction against globalization and marketization. Instead, I suspect that the relationship is more complex than that. For much of the Soviet periphery, the process of Soviet-era industrialization was also the process of Russification. Many of the refineries, mines and steel towns of the now “near-abroad” were built by and for Russian laborers induced or forced to relocate to the non-Russian republics. It was this dual-pronged Stalinist strategy of simultaneous industrialization of the economies and Russification of the populations which was to ensure the integration and interdependence of the Soviet republics, and which came to ensure, ironically, the future marginalization of those transplanted Russian populations. It is this peculiar legacy of the Soviet experiment that yields the strange bedfellows of post-Soviet coalitions.

The nature of post-Soviet coalitions also calls into question the conventional wisdom regarding the role of economic sectors in modernization and economic opening. The agricultural sector is often assumed to be the seat of regressive and fascistic movements, while industry is to provide the impetus for modernization and liberalization. While it may be true that nationalism is stronger in many of the rural regions of this study, it is also true that *industry* has proven the backbone of protectionist, anti-liberal coalitions. Just as the post-Soviet cases force us to examine our assumptions about the place of nationalism in a protectionist/liberalizing dichotomy, so must we examine more closely broad assumptions about the roles of specific sectors. Social coalitions, and cleavages, are the products of their specific historical and institutional contexts. It is for

this reason that process-tracing is essential to our understanding of the origins of such coalitions.

It is also a legacy of Stalinist industrialization that gave rise to one of the central dilemmas facing these new states, that is, of energy dependence on Russia. The industrial structure of the Soviet Union has sometimes been compared to the import-substituting industrialization adopted in other regions of the globe. To be sure, ISI and Soviet socialist industrialization share many characteristics, not least of which are the economic inefficiencies which begin to breed in these sectors and the networks of actors who benefit from their preservation. Stalinist industrial industrialization had other lasting legacies, however: the “gigantism,” overspecialization, geographical dispersion, and inefficient use of energy resources served to knit the republics of the Union into a highly interdependent economic web. It is this interdependence, and particularly many NIS’ energy dependence, which may be the most difficult legacy to overcome.

The findings of this study must also make us question the relationship between economic and political reform and liberalization. “Transitologists” have batted around the questions of the relationship between economic and political reform, if one necessitates the other, and if they happen in sequence, which sequence makes for a more successful transition. Perhaps it would be more comfortable to argue that political reform and democratization must take place first, that citizens must be ensured of their rights before a market can function freely. The findings of this study suggest that this is not necessarily so. The globalizers, Estonia and Latvia, realized the most successful economic reforms and transformation while also establishing decidedly undemocratic and

exclusionary suffrage laws. The good news for the Russophones of the northern Baltic states is that the Western aspirations of Latvia and Estonia will probably drive them to extend the democratic franchise to all residents: much-valued membership in bodies like the European Union may depend on it. In addition, some recent work suggests that the most liberal forms of citizenship were formed when citizenship was exclusionary, such as the case of the United States and the disenfranchisement of women and African Americans.<sup>16</sup> Perhaps all the Russophones of the Baltics will need is patience and perseverance.

However, one cannot argue that a lack of democratic political reform necessitates a successful marketization. Our Russophile is a case in point: the most undemocratic of the states is also the least reformed economically. I would argue that the priorities of the state cannot be assumed. One must first know the origins and policy preferences of the ruling coalition before one can deduce the use the state will make of its measure of political autonomy.

Lastly, we must perhaps ask by what yardstick we measure the success of “transition.” This study might easily be misread as unrestrained praise of the globalizer model, and an indictment of the backwardness of the Russophile path. The findings are more nuanced, however. Clearly, the globalizers have realized success of which their NIS neighbors only dream: establishment of the rule of law and stable political institutions, high rates of growth and foreign investment, successful structural and industrial restructuring, the growth of dynamic new, more efficient economic sectors,

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<sup>16</sup> Rogers M. Smith, *Civic Ideals: Conflicting Visions of Citizenship in U.S. History* (New Haven,

growing economic autonomy from Russia, and growing acceptance into the international community of nations. These are, not surprisingly, outcomes valued by the “right”. These advances have not been without their costs, however; these states suffer criticism (and justly so) for the political exclusion of large portions of their populations. While their political institutions may be stable, they are not entirely democratic. These structural economic adjustments were also quite difficult for the persons displaced, leading to high rates of unemployment. These economies which engage the process of globalization experience other difficulties with which we ourselves are familiar: a growing gap between rich and poor, between the unemployed and the workers in the new sectors, between the haves and have-nots.

The problems inherent in the Russophile strategy are many, and need not be fully recounted here. However, Belarus has managed to avoid many of the pitfalls of the globalizers. Employment rates remain high, even if jobs are often superfluous and ill-compensated. Because there has not been the massive sectoral restructuring and therefore social displacement experienced in the globalizers, GDP did not experience the same magnitude of decline. While the standard of living remains low, there is a level below which citizens are not allowed to fall. The social security net remains intact, providing pensions, child-rearing subsidies, and other perks which keep the citizens on an even footing. These are essentially, and unsurprisingly, “left” values.

The model that seems to have failed on both counts, neither dramatically restructuring the economy and laying the groundwork for a new, dynamic system, nor

preserving the stability and standard of living of the status quo, is that of the hybrid. These states have experienced economic decline, but with less hope of preserving the safety net or of experiencing a rapid recovery. In some way, however, the failure to consolidate a consistent economic and energy policy in these states is a result of democracy itself. The obstacles to reform in post-Soviet states are many and well known. In addition to these, however, the states in the hybrids, unlike those in the Russophile or the globalizers, attempted to accommodate both the winners and losers under economic reform and globalization, and this was a source of their weakness.

Again we must return to the question of the measurement of success, however. Is it economic growth or economic stability, national autonomy from a former colonizer or an open and representative political process? While Belarus may have maintained greater economic stability and even growth than, for instance, Ukraine, can it be said to be a greater success in terms of the freedom of its people? Just as Estonia and Latvia surged ahead of their southern neighbor, Lithuania, in economic terms, must they not be said to lag behind in measures of democracy? Before we can evaluate the success of these transitions, we must first decide the value of political freedom. This begs the question of the priorities of the policy-makers themselves, however. The relative weight we place on economic versus political reform may indeed be irrelevant to the ruling political coalitions' policy priorities of state independence, energy security, or simply the protection of the status quo.

The cases of the hybrids may indeed prove the most interesting. First, to call them intermediates or gradualists assumes an inevitable march toward some other category. But as the post-Soviet era drags on, we find that many so-called “transitional economies” (not to mention “developing economies” or “emerging markets”) are not so much transitioning to a new (and, of course, liberal) state, but rather plateauing in a state of political compromise or near-chaos, economic stagnation and geopolitical marginalization. This indeed seems to be a growing and seemingly semi-permanent category of nations. This group of states, more than those who join the industrialized West and those who seek to avoid change altogether, may prove the most analytically interesting and challenging.

The question of energy dependence for these nations is related to the question of sovereignty itself. Most of the leaders of these small states, caught between great powers, understand that their states could not hope to go it alone in the international arena any more than these natural resource-poor nations could aspire to energy autarky. How could they ensure the independence of their state, when they were necessarily dependent on another for the lifeblood of their economies? Some sought refuge in the faceless global economy, reasoning that to attain the ability to pay world market prices freed the state of reliance on any single supplier. However, achieving this ability would not be without its costs domestically, and the volatility of the global market would introduce a different kind of insecurity. Others chose security over independence, offering to cede sovereignty itself in exchange for the stability of subsidies and shelter from the “creative destruction” of the global market. This strategy has sustained them for now, though they may

eventually find their shelter to be a house of cards. Still others were unable to find the consensus to pursue consistently one strategy or the other, and found themselves simultaneously buffeted by economic shocks at the same time that they remained strangely answerable to their energy supplier. Theirs has perhaps been the most difficult path of all.

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## II. INTERVIEWS

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Dostanko, Elena Anatol'eva, Ph.D., Vice Dean, International Relations Department, Belarusian State University. Interviews with author, October 6, 7 and 8, 1999, Minsk, Belarus.

Gagilas, Vladas, Director, Energy Resources Department, Ministry of Economy, Republic of Lithuania. Interview with author, October 14, 1999, Vilnius, Lithuania.

Gordeichik, Aleksandr Ivanovich, Ministry of Foreign Affairs, Republic of Belarus. Interview with author, October 7, 1999, Minsk, Belarus.

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Kazlauskas, Jonas-Rimantas, Ph.D., Director, Energy Development Department, Ministry of Economy, Republic of Lithuania. Interview with author, October 12, 1999, Vilnius, Lithuania.

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- Lauri, Hillar. Director Estonian Operations, NRG Energy International. Interview with author, October 18, 1999, Tallinn, Estonia.
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Slavenas, Erikas. Acting Head, European Integration Department, Division of Political Cooperation, Ministry of Foreign affairs, Republic of Lithuania. Interview with author, October 11, 1999, Vilnius, Lithuania.

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Vasylevich, Vladimir P., Technical Director, Plastma Ltd. Interview with author, October 6, 1999, Minsk, Belarus.

Vinciunas, Arunas, Head of Regional Economic Analysis Division (Russia and CIS), Ministry of Foreign Affairs, Republic of Lithuania. Interview with author, October 12, 1999, Vilnius, Lithuania.

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*Power and Uneven Globalization: Coalitions and Energy Trade Dependence in the Newly Independent States of Europe*, Dissertation, University of Washington, August 2000.

"Politics and Power: Baltic-Russian Energy Trade and Policy," for the American Association for the Advancement of Slavic Studies, 31st National Convention, St. Louis, Missouri, November 18-21, 1999.

*The Politics of Regional Energy Trade in the Newly Independent States*, panel organizer, American Association for the Advancement of Slavic Studies, 31st National Convention, St. Louis, Missouri, November 20, 1999.

"Defining the National Interest: Social Forces and Energy Trade Policy in the Newly Independent States of Europe," poster for American Political Science Association, 95th Annual Convention, Atlanta, Georgia, September 2-5, 1999.

"Agent Mobility and the Evolution of Cooperative Communities," Stephen Majeski, Greg Linden, Corina Linden and Aaron Spitzer, *Complexity*, Vol 5:1, 1999, 16-24.

*Structural Adjustments, Integration, and Promoting Democratic Values*, discussant, Western Political Science Association, Annual Meeting, Seattle, Washington, March 25-27, 1999.

"Paradox of the Periphery: the Effects of the Structure of Soviet Regional Politics on State Strength and Market Reform in Post-Soviet Russia," Master of Arts Essay of Distinction, University of Washington, January 1996.

"A Spatial Iterated Prisoners Dilemma Game Simulation with Movement," S. Majeski, G. Linden, C. Linden and A. Spitzer, in R. Conte, R. Hegselman, and P. Terna, eds., *Simulating Social Phenomena*, Berlin: Springer-Verlag, 1997, pp. 161-167. Presented at the International Conference on Computer Simulation and the Social Science, September 22-5, 1997, Cortona, Italy.

"SimSociety: A Spatial Iterated Prisoner's Dilemma Simulation with Movement" S. Majeski, G. Linden, C. Linden and A. Spitzer, Economic Science Association Conference, October 17-20, 1996, Tucson, Arizona.

"Essentials of Evolutionary Thought in the Social Sciences: An Annotated Bibliography" with George Modelski and David Wallerstein, 1995.

*Evolutionary Paradigms in the Social Sciences II*, with George Modelski, Report of workshop held May 26-27, 1995, University of Washington, Seattle.

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Administrative Assistant, University of Washington, Winter 1994

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#### Independent Teaching

PolSci 203 Introduction to International Relations, UW, Winter 1999

PolSci 203 Introduction to International Relations, UW, Summer 1998

US Citizenship Classes, Jewish Family Service, Summer 1997

Taught courses to political and religious refugees from the former Soviet Union in US civics, government and English language. Conducted classes in Russian and in English.

#### Teaching Assistantships – University of Washington

JSIS 401 Theories of International Political Economy  
(Autumn 1997, Autumn 1996, Autumn 1995)

PolSci 203 Introduction to International Relations  
(Spring 1995, Winter 1995, Autumn 1994)

#### Pedagogical Coursework – University of Washington

JSIS 580 Teaching International Studies, Winter 1995

PolSci 597 Teaching Political Science, Autumn 1994

### **FELLOWSHIPS, AWARDS AND HONORS**

Foreign Language and Area Studies Fellowship, University of Washington, United States Department of Education

1996 Winter - 1996 Spring

1996 Autumn - 1997 Spring

1997 Autumn - 1998 Spring

1998 Autumn - 1999 Spring

Regents Scholarship, 1989-1993, University of California at San Diego

Provost's Honors List, 1989-1993, University of California at San Diego

United States Information Agency Scholarship, 1992

### **PROFESSIONAL MEMBERSHIPS**

Graduate and Professional Student Senate, University of Washington.

Departmental Senator 1998-1999, 1999-2000.

American Association for the Advancement of Slavic Studies

American Political Science Association

Society of Women in International Political Economy

Western Political Science Association