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energy capital



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China's One Belt One Road  
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# BALTIC RIM ECONOMIES

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OLAVI ALA-NISSILÄ

# Baltic Sea countries can offer lessons and boost to Finnish economy

Expert article • 2128

Six years ago the members of the European Court of Auditors had a seminar in Tallinn. The then-prime minister, Andrup Ansip, told us lessons from the Estonia's history.

He reminded how - after restoring the independence - Estonia had joined the Nato, the EU and the Euroarea as soon as it was possible. But this was never enough for us, he stressed. We wanted to be economically independent as well. That was why we decided that we cannot live beyond our means, Ansip told us. And as a consequence, Estonia practically does not have any public debt (10,1 percent of GDP by the end of 2015 whereas Euroarea average was more than 90 percent of GDP).

Another example comes from Latvia. The country and its citizens did live beyond their means as it tried to catch up with the rest of the EU way too fast. The economy overheated and then collapsed suddenly at the end of 2008. The country was forced to accept help from the EU and the IMF under strict conditions. But, unlike some other bailed-out countries, Latvia did put its house back in order in record time. The then-prime minister Valdis Dombrovskis did not hesitate to cut public expenditure and implement reforms. The confidence came back, as did the economic growth and the country could start paying back to its creditors earlier than originally agreed.

Poland with its 40 million people has huge potential. The country has relatively young and growing population hungry for learning and earning. It is the only EU member state which has grown every single year since the financial crisis started in 2007. The importance of Poland was reflected recently as Finnish prime minister Juha Sipilä made his first state visit of year 2017 to Poland.

In Germany, Sweden and Denmark the structural reforms especially in labor market have brought significant benefits to their economies. Unemployment rates in those countries are among the lowest in the EU. Not so long time ago, Germany used to be called the sick man of the Europe. How quickly things can change, when the politicians have the courage to act in the best interest of their country!

The Baltic Sea is EU Sea. Eight EU member states are situated around the Baltic Sea. Not to mention Russia and its second biggest city, St Petersburg. Security issues in the Baltic Sea area are making

headlines almost on daily basis. But, the area is economic heavy weight as well.

At the moment, the Baltic Sea area is boosting Finnish economy through many channels. German shipyard in Turku has won several contracts and the orders are keeping it busy for the next ten years. In Uusikaupunki, automotive industry is doing its best to keep up with increased demand for new jobs. Travelling between Finland and Estonia hit a

new record last year. Even the Russian tourists seem to be coming back to boost sales in Helsinki and Eastern parts of Finland.

There is an old Finnish proverb which says that one should not reach too far to go fishing. In concrete terms, the good place to start fishing is the Baltic Sea. ■

Poland with its 40 million people has huge potential. The country has relatively young and growing population hungry for learning and earning. It is the only EU member state which has grown every single year since the financial crisis started in 2007.



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Member of Grand Committee  
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Court of Auditors

SOLVITA ĀBOLTIŅA

# The evolution of cyber security threats

Expert article • 2129

Every year the development and progress of modern technologies brings about ever greater threats and risks to global security. The cyber threats we face today force us to accept that security is not something we can take for granted. In response to increasingly complex threats, NATO has declared that, depending on their severity, cyber-attacks could trigger Article 5 of the North Atlantic Treaty. This is not surprising, taking into consideration the damage that can be caused today through illegal use, tampering, paralyzing or the destruction of various information and communication technologies.

The Baltic States also have their share of experience in this area. In 2007, Estonia was the target of one of the most well-known Russian supported and funded cyber-attacks, which blocked data transmission networks of state institutions and the media. This was a serious lesson for the entire region, prompting Latvia to revisit its assumptions about the vulnerability of the virtual space and the need for increased cyber security. Since then, the Baltic States have had to deal with cyber-attacks of varying severity on a regular basis; therefore, nowadays strengthening national cyber security has become an indisputable priority in Latvia both at the policy-making and the legislative level. A proper cyber security management structure and legal framework has been established, and short-term and long-term targets have been set. During the development of this year's budget, the government and parliament placed security and defence, including cyber security, as absolute priorities. According to the government's decision to increase defence spending, the proportion of GDP allocated to defence is estimated to be 1.7% in 2017 and no less than 2 percent in 2018 and the following years. This demonstrates that Latvia as a state is aware of the threats existing in cyberspace, and is already taking concrete steps to ensure that, when necessary, decision-makers can quickly and objectively assess and analyse arising threats, and consequently take deliberate steps with a long-term vision at the national level.

Within the current global reality it is clear that hybrid warfare makes use of not only misinformation and large-scale propaganda campaigns, but also cyber-attacks with the aim of influencing the internal affairs of other countries, their decision-makers and even such democratic processes as elections. Events around the world last year – the UK referendum on leaving the EU in the summer, the US presidential elections in the autumn – have been a jolt for the international community, prompting it to devote more effort to developing online defence capabilities. And with good reason – the presence and interference of Russian cyber forces were found to have been extremely likely in both cases. This experience teaches us one thing: today no country is safe from Russia's attempts to increase its international influence through ever more innovative manipulation, including cyber-attacks. Latvia must take this into consideration as it prepares for the upcoming local government elections this year and the parliamentary elections next year. We have to be able to do everything possible in order to duly and proactively respond to similar attacks and prevent Latvian society from being dragged into a hybrid war. We must not allow outside forces to influence the minds of our

people, just as we must be able to respond and counter any attacks on state institutions, infrastructure and public opinion.

In this context, one of the most important takeaways of the 2016 NATO Warsaw Summit was the decision that cyberspace is an operational space equal to land, air and sea. At this time when cyber threats in the region are becoming increasingly visible and present, the only potentially effective solution and response is ever closer cooperation with our partners and allies. Sharing experience by learning from the conclusions that our partners and neighbours have drawn from cyber-attacks, as well as from the cyber defence strategies that they have implemented, and by holding exercises to improve our cyber defence capabilities, we will be able to significantly heighten our ability to prevent incidents and crisis situations.

It is our duty to defend our people and to ensure that they are properly informed and critical towards information surrounding them. Awareness about cyber security needs to be increased not only within the state administration, but also in schools; children and youth must be taught from the very outset how to navigate the immense flow of information, so that they are able to verify it or know how to select trustworthy sources. We have to teach children how to separate facts from manipulative opinions, and explain to them the importance of their own data security in the Information Age.

With regard to cyber security, we must keep reminding ourselves that the best weapon against cyber threats is intelligence and critical minds that do not yield to provocation, deception and confusion. The only sustainable solution for the future is promoting critical thinking, improving analytical skills and raising media literacy. This is just as important as the continued efforts of the state to ensure its national security. We cannot depend on our allies and Article 5 alone; we need to be able to defend ourselves in cyberspace just the same as at our national borders. ■



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MATS LÖFSTRÖM

# The need for longer perspectives in a fast moving world

Expert article • 2130

**T**he autonomous Swedish speaking Åland Islands, geographically located between Finland and Sweden are today known as the Islands of Peace. The islands are demilitarised and neutralised by several layers of international treaties. The first treaty of its demilitarisation is older than the Finnish independence.

The life on the windy islands in the Baltic Sea has mostly been very peaceful, but not in the summer of 1854. After being a part of Sweden throughout the history since the founding of national states, Sweden lost the islands to the Russian Empire in 1809. Russia started to build the fortress of Bomarsund in the northern parts of the main island. However the fortress was only half-completed at the start of the Crimean War. In the summer of 1854 an Anglo-French armada with battle ships and 30 000 soldiers reached the islands, bombarded the fortress and landed soldiers. The fortress commander Jacob Bodisco surrendered the fortress 16th of August 1854 and it was decided that the fortress should be destroyed.

The Treaty of Paris in 1856 put an end to the Crimean War and the Convention annexed thereto demilitarised the Åland Islands despite the fact that the islands continued to be under Russian control. This is the first layer of international treaties stipulating the demilitarisation of the Åland Islands.

In 1917, Finland dreamt of and planned for independence. At the same time Åland Islands dreamt of and planned for a reunification with Sweden. The Finnish independence didn't stop the Åland movement wanting a reunification with Sweden. The Finnish Parliament offered the Åland Islands autonomy in 1918. The offer was turned down since Åland didn't want to be self-governed, but wanted to be a part of Sweden. This dispute was therefore brought in front of the League of Nations, the predecessor of today's United Nations. The League of Nations resolved the dispute, which meant that the Åland Islands became an autonomous Swedish speaking part of Finland. Separately a convention on the non-fortification and neutralisation of the Åland Islands was agreed. This is the second layer of international treaties stipulating the demilitarisation, and also Åland's neutralisation. The treaty is designed in a way to last eternally since it includes an article that stipulates that the provisions of the convention shall remain in force in spite of any changes that may take place in the present status quo in the Baltic Sea.

The third layer of Åland's demilitarisation is the 1940s treaty of Moscow between Finland and the Soviet Union. The treaty is confirmed in accordance with the Paris peace treaty in 1947. The Paris peace treaty also stipulated that the Åland Islands shall remain demilitarised in accordance with the situation as at present existing. In the Moscow treaty there is an article that also gives the Soviet Union the right to keep a consulate on the Åland Islands, with the task to monitor that the islands do not get fortified. Russia still has this consulate on Åland with special rights to, under some circumstances, request meetings with the governor of Åland.

In the autumn 2016 there was a discussion in the Finnish public debate and the media regarding Åland's demilitarisation. When I was giving comments and interviews on the matter, I was a bit puzzled over how little the legal framework and the international treaties of the island's status was known to the wider public. One journalist who was doing research asked me what I would think of Finland cancelling the agreements and fortifying the islands. The person thought Åland's demilitarisation was an agreement only between Finland and the Åland Islands.

Finland cannot unilaterally change Åland's demilitarised status as it is a multilateral arrangement. Furthermore, it is not in Finland's interest to do so and it is not in line with Finnish diplomatic tradition. We don't cancel international agreements, we follow them. Secondly, and hypothetically, if Finland would withdraw from international agreements regarding the Åland demilitarisation the agreements would still be in force and Finland would breach international law if fortifying Åland. The status of the Åland Islands has also become regional customary law, which means that it is binding also on states in the region not party to the agreements.

In the general debate it is sometimes said that it would be naïve to think that Åland's demilitarisation would save Åland from a military conflict and that the non-fortification treaty doesn't make it easier for the Finnish military to defend Åland's demilitarisation.

Finland has the right and obligation to defend Åland's demilitarisation, also with military force. But, it was never Åland or Finland alone that decided that Åland should be demilitarised.

Countries cannot choose which countries they would like to have as their neighbours. Countries need to accept and live with the neighbours they have, even though a neighbour can get aggressive with one of its other neighbours. This is the reality we live in and this is the reality for Åland's demilitarisation as well. It is there. It is in place.

Finland is a small country in the world. History has learned that respecting and underlining the need for international law is a crucial defence for smaller countries. Without international law, only the strongest would decide. It is certainly not in Finland's interest that the world order becomes a rough school yard where the strong can bully the weak. Therefore, it is of paramount importance that Finland stands behind international obligations.

It is important not to be naïve in a world where the security level in, and around, the Baltic Sea is deteriorating. At the same time, it is important to have the historical perspectives in place and not overreact. ■

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LAIMDOTA STRAUJUMA

# Sustainable development of Latvia

Expert article • 2131

The world is increasingly interconnected, fast moving and unpredictable. The opportunities and threats we face are constantly evolving. Europeans expect their governments to create jobs, generate wealth and provide security. At the same time, the state's ability to deliver is limited by economic realities and the uncertainty of international environment. We face a new political dynamic: the changing public attitude towards government bodies. This shift has manifested itself in numerous ways and created a complex picture across Europe and the entire world.

Latvia is an open economy with a population of around 2 million. We have made significant progress after re-gaining independence in 1990. Latvia joined the WTO, the EU and NATO, the Euro area and the OECD. The main national long-term development planning document – Sustainable Development Strategy of Latvia until 2030<sup>1</sup> – has been approved by the Parliament of Latvia.

The basic idea of sustainable development invites to meet the needs of the present generation, balancing public welfare, environmental and economic development interests, in order to avoid the reduction of possibilities of future generations. Seven priorities are determined in Latvia 2030.

**1. Development of Culture Space.** It is important for Latvia as a small nation to preserve and develop its cultural capital and to promote a sense of belonging to the cultural space of Latvia, its identity, language, values of national culture and lifestyle, based on the creativity of the society.

**2. Investments in Human Capital.** To counter the decreasing population and the ageing society in the country, it is essential not to reduce the base value of human capital. Our objectives are to increase the productivity of human capital and to reduce social inequality. Formation of an advanced lifelong learning system and improvements in the healthcare system are our nearest future development directions.

**3. Changing the Paradigm in Education.** Educational attainment and skills have a strong influence on labour market outcomes and the capacity of any country. The shift in the education paradigm will provide a closer link between the education system and economic and public processes. It will promote the use of information technologies, as well as a synergy between general and vocational educational institutions and institutions of higher education.

**4. Innovative and Eco-Efficient Economy.** Upon increase in the costs of labour, Latvia is losing its economic advantage. Support for the creation and commercialisation of new ideas, knowledge transfer and user-directed research are incentives to be developed. We will pave the way to create better conditions for business investments aiming to generate high-value-added products. Another important task is to ensure energy independence of the state by increasing the provision of clean energy resources and integration in the EU energy networks.

**5. Nature as Future Capital.** The most valuable natural resources of Latvia are biological diversity, water, air and the unique landscape. Latvia is one of the best preserved sanctuaries for wild animals. Our environment is priceless. Our objective is the preservation, increase and sustainable use of natural capital.

**6. Spatial Development Perspective.** Equivalent life and work conditions are crucial for all persons regardless of their place of residence. A polycentric state development structure has been defined. Good accessibility is a decisive precondition for a balanced development of regions and the global competitiveness of the state. The development of the transport infrastructure and communication networks will provide opportunities for regions and ensure the possibility

for Latvia to become a significant transit hub.

**7. Innovative Government and Public Participation.**

An efficient public administration should be capable not only to respond quickly to changes, but also foresee and guide them. We are strong supporters of the 'digital by default' principle. Our direction is more E-government

and more state and local government services following the 'one stop shop' principle. Businesses are stifled by the red tape, and we must make regulatory procedures less cumbersome. The efficiency and quality of the judicial system has improved over the past years, though challenges remain. We have to work further on insolvency regulation and court reforms.

In order to stick to our plans, structural reforms need to be continued. They should be decisive and fast. We are making progress. But we should be frank – the job is not done yet. Economic growth balanced with an effective social system, - is the course that we are pursuing to ensure sustainable development of Latvia. ■

The basic idea of sustainable development invites to meet the needs of the present generation, balancing public welfare, environmental and economic development interests, in order to avoid the reduction of possibilities of future generations.



LAIMDOTA STRAUJUMA

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<sup>1</sup> [Sustainable Development Strategy of Latvia until 2030](#)

JOAKIM STRAND

# Vaasa - the Nordic energy capital

Expert article • 2132

**T**he City of Vaasa is a successful seaport, and it is well known for its unique archipelago, bilingualism and a colourful history. The Kvarken archipelago just outside Vaasa forms a World Heritage area together with the Höga Kusten area in Sweden, and is the first UNESCO Nature Heritage Site of Finland.

The maritime location and good means of communications have created a tradition of active entrepreneurship and export trade. Also the bilingualism has offered a strong base for international markets. The Vaasa region is in fact one of the most international regions of Finland. The region has always been open to new ideas and people, and Vaasa alone has inhabitants representing over 120 nationalities.

The companies are doing a lot of cooperation with the educational sector in the region. Compared with the amount of inhabitants, Vaasa is the biggest university city in Finland. There are 13 000 students in six different units of higher education, and education is available in Finnish, Swedish and English. The strong cooperation between the institutions of higher education and the companies guarantees good employment possibilities for the students and offers competent manpower for the companies in the future.

## The gold coast of export

The high export rate and good employment levels describe the area well. We have the highest amount of export companies in relation to the number of inhabitants and the export rate per capita is top-notch. More than 80 percent of the production in the area is exported.

The Vaasa region is the biggest energy cluster in the Nordic countries: we employ 12 000 persons and we are responsible for more than 30 percent of the whole export in the energy technology industry in Finland - even though only two percent of the country's inhabitants live in the Vaasa region. In total there are over 140 companies in the regional energy cluster, with the biggest being ABB and Wärtsilä. Their combined turnover is around € 5 billion. In other words - it's a real gold coast in terms of exports.

The private sector of the energy cluster yearly invests about €200 million on research and product development. The Vaasa region is one of the most important areas for research and development in Finland. The Finnish government has given Vaasa the task to lead the development of sustainable energy solutions in the whole country. The task has a world wide range: we shall develop platforms for solutions that work anywhere in the world.

Vaasa has committed itself to several international, national and regional projects and agreements aimed at reducing the strain on the environment and increasing energy efficiency. We also wish to bring the energy competence as a part of the inhabitants of Vaasa already from childhood. The target is to bring energy and sustainable development as a natural part of the teaching and learning environments and increase the energy consciousness, interest and passion.

The new research and innovation centre within the energy field, VEBIC - Vaasa Energy Business Innovation Centre, supports the development of the energy business field in Vaasa. Big combustion engines will be placed in the research and product development laboratories in the University Campus. These engines will be used when testing the use of different fuels.

## Midway Alignment

This year Vaasa also navigates strongly forward through the international *Midway Alignment of the Bothnian Corridor* project. One of the big targets of the project is to build a new innovative ferry for the traffic over Kvarken in the Gulf of Bothnia.

The common project for the Vaasa and Umeå regions strives to strengthen the traffic network of Europe and adding the competitiveness in the Kvarken area by developing a transport route which crosses the Finnish and Swedish borders. The harbour of Vaasa is already now an important part of the Nordic Logistics route, which reaches all the way from the Norwegian

harbours to the European and Russian transport routes.

Midway Alignment combines with three due to UNECE classifications strategically important European arterial roads (E12, E4 and E8) as well as the Bothnia route. It also complements the most important traffic projects of the EU and the exhaustive traffic network defined by the EU.

## The ambitious Gigafactory project

Vaasa has also decided to apply for the billion class Tesla factory, Gigafactory, which produces lithium-ion batteries. Tesla's first Gigafactory was opened in Nevada, USA in July 2016. Tesla has announced their intention to build their next Gigafactory in Europe.

The advantage of Vaasa as a location is that it is the most important energy technology centre in the Nordic countries. Kaustinen, which lies nearby, has the biggest lithium deposits in Europe. Lithium carbonate is the key ingredient in lithium-ion batteries. This combination of knowledge of energy technology and supply of the raw materials for battery production is unique in the world. The energy cluster in Vaasa and Tesla has a common target: to speed up the world's transition to sustainable energy. ■

The Vaasa region is the biggest energy cluster in the Nordic countries: we employ 12 000 persons and we are responsible for more than 30 percent of the whole export in the energy technology industry in Finland



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Finland

VALDEMARAS SARAPINAS

# Lithuania and Finland: shoulder to shoulder in ensuring security for themselves and the whole region

Expert article • 2133

Lithuania and Finland, two Nordic-Baltic sisters, are interconnected by long-ranging historical, political, and cultural links. It is great to state the fact that Lithuania and Finland have truly deep cooperation traditions. Relations with Finland and other Nordic countries are of strategic importance for Lithuania. Last year we celebrated the 25th anniversary of re-established diplomatic relations between Lithuania and Finland after Lithuania restored its independence on March 11, 1990. Finland was the sixth country in the world to renew diplomatic relations with Lithuania. This year Finland and next year Lithuania will celebrate 100-year anniversary of independence, and both countries will commemorate these occasions with many meaningful projects and events. Recent official visit (last October) of the Lithuanian President Dalia Grybauskaitė to Finland contributed to the strengthening of bilateral relations. So, Lithuania and Finland are closely related in many areas.

Today, however, the most important link that connects our countries is the closest possible cooperation in security and defense as it's currently a number one issue. The geopolitical situation remains intense as Russia's military activity is not decreasing. It is continuously being demonstrated by carrying out large-scale snap exercises, infringing airspace, impeding the movement of ships in the Baltic Sea and occasionally placing Iskander ballistic missile systems in the Kaliningrad region.

Evidently, Russia is continuously testing our solidarity on daily basis. That's why we, countries of the region, must always demonstrate team spirit in everything we do: NATO countries in implementing Warsaw Summit decisions, EU countries in strengthening EU defense cooperation as well as imposing sanctions on Russia. In that same spirit of unity, we should remain open to meaningful and value-driven dialogue with Russian Federation.

Being an active participant of NATO Enhanced Opportunities Programme, Finland actively contributes to strengthening the security of the Baltic countries. Finnish troops constantly participate in common military exercises, their F-18 fighters, together with NATO air police mission fighters, take part in the Baltic Regional Training Event, and both countries regularly exchange information in monitoring the air and sea space, which undoubtedly contributes to more effective air space surveillance over the Baltic Sea and the neighborhood of NATO countries.

This year Finland leads the NORDEFECO (Nordic Defense Cooperation) and Lithuania is invited to actively join the military projects of the Nordic countries. The Lithuanian Navy is taking over Finland's

experience in creating and improving an integrated sea surveillance system in Lithuania. Another example of our fruitful cooperation is the NATO Energy Security Center of Excellence, operating in Lithuania. Finland gladly agreed to join the activities of the Center by sending its representative there.

Lithuania has been a member of the world's most powerful alliance for more than twelve years. Therefore, just like other members of the Alliance, it has both the guarantees of NATO collective defense as well as its responsibilities and obligations. It is great to see that the security and deterrence measures adopted in Warsaw are being rapidly implemented. However, we understand that firstly we, ourselves, are responsible for the defense of our own country. Finland in this respect serves as an excellent example of how to take care of its own security and defense.

All of this became even more relevant after Russia's aggression in Ukraine, which made both of our countries concerned even more about our security and defense. The concept of territorial defense once again became relevant. Lithuania, following the Finnish example, decided to strengthen its armed forces by reinstating the conscription system. At the same time, this is an effective way to form our military reserve faster. The younger generation in Lithuania was extremely positive about this decision - from the very beginning we had more volunteers ready to serve than we can accept at this moment. The society is also supportive of this decision, which undoubtedly contributes to developing the feelings of patriotism, public spirit, and responsibility of our young people.

The political situation, which recently has become more severe, served as a stimulus for both countries to increase their defense expenditures. In Lithuania during the last two years it has increased by 60%. This year it amounts to 1.8% of the GDP, and will reach 2% in 2018.

Lithuania is also continuously seeking to improve the readiness of its armed forces. The best example of that is the establishing of high readiness forces, which are ready to react to a threat within hours, not days or weeks. In addition, last year we have established one more brigade in our land forces.

Last year Lithuanian State Defense Council approved the new Military Strategy, which also strongly reflects the elements of hybrid warfare, encompassing a variety of areas – the fight against cyber, disinformation, and energy threats and migration challenges. Therefore, Lithuania compliments Finland on its initiative and decision to establish the European Center of Excellence for Countering Hybrid

Expert article • 2133

Threats. Understanding its importance, Lithuania is ready to contribute to the Center's operation since the very beginning. Moreover, Lithuania also amended the law to allow the use of military force during the peacetime, which is exactly what our Finnish colleagues are now preparing to do.

Seeking to modernize their armed forces, both Finland and Lithuania are planning very solid acquisitions. Finland is thoroughly preparing to implement the projects of replacing the F-18 fighters and acquiring war ships. For Lithuania, the most important projects are the acquisition of self-propelled howitzers, infantry fighting vehicles, medium range anti-tank and medium range air defense weapons. Furthermore, Finland continues to successfully develop national military industry.

So as paradoxical as it may seem, Russia's targeted policy and the current intense security situation in the region served as a new impulse for a closer Lithuanian and Finnish military cooperation, which, hopefully, will continue successfully in the future and contribute to ensuring security and stability in the whole region. ■



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# BALTIC RIM ECONOMIES

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**BRE**  
REVIEW

EDWARD HUNTER CHRISTIE

# Russia's challenge to the security of NATO allies and partners in Northeast Europe

Expert article • 2134

The last three years have brought enormous change to the security landscape of NATO Allies and Partners in Northeast Europe. The Russian Federation's aggressive actions against Ukraine mark a clear break with any past attempts at forging a sustainable partnership with Moscow. In demonstrating both the means and the will to use military force as a tool of its foreign policy, Russia has forced the NATO Alliance to refocus on its core mission – deterrence and defense of its home territories.

In order to strengthen deterrence and defense while simultaneously demonstrating to Moscow that no actual threat could possibly be posed towards Russian territory, Allied governments have deliberately settled for a new but quantitatively small forward presence in the region, formally referred to as NATO's Enhanced Forward Presence. This consists of four multi-national battalions, in Estonia, Latvia, Lithuania, and Poland, respectively. These battalions will be under NATO command and should be fully in place before the summer of 2017. A battalion has approximately one thousand service personnel. As a result, the scale and scope of these forces unambiguously mark them out as defensive in nature. The Russian Federation *knows* that they are defensive by observing their characteristics.

Russia's posture, on the other hand, is not unambiguously defensive. The nation's development of anti-access/area denial (A2/AD) capabilities, in the region and elsewhere, could be consistent with an offensive posture. A2/AD systems could be used to help shield a Russian attack against NATO Allies, in order to strike at Allied reinforcements that would be making their way to the region to respond to such an initial attack, as well as at Allied territory more broadly.

Another consideration is military exercises: in recent years, Russia has conducted exercises that far exceed, in both size and scope, any recent NATO or other Allied exercises in Europe. In parallel, Russia has invested very substantial sums in modernizing and upgrading its armed forces. Estimates suggest that military procurement spending alone has exceeded 2% of GDP in 2014, 2015, and 2016. For NATO Europe as a whole, the equivalent figure has been less than 0.4% of GDP in each of the same years. Correcting for price differences, Russia's recent procurement levels are estimated to be in the same order of magnitude as those of the whole of Europe put together. A partial slowdown to Russia's spending effort is expected, in light of the recently approved federal budget. However procurement levels are expected to remain high.

While the military picture is clear for any objective observer, Russia nevertheless seeks to undermine the Alliance's cohesion, its resolve to defend itself, and its desire to uphold strong links of partnership, notably with Finland and Sweden, in support of its defensive posture in the region.

In doing so, Russia can rely on an extensive range of non-military instruments of coercion and subversion. A recent article in the *Journal of Strategic Studies*, by Martin Kragh and Sebastian Asberg, details some of the methods Russia has deployed in the particular case of Sweden. Russia's overt propaganda efforts, for instance using state propaganda and disinformation outlets such as Sputnik or RT (formally Russia Today), are well documented. There is also an increasing awareness of Russia's deployment of covert (if increasingly obvious) 'trolls' and 'bots' to artificially boost the online visibility of Kremlin-friendly content. Kragh and Asberg also highlight cases of traditional, Soviet-style 'active measures'. Their article highlights 26 cases of forgeries or fake news items, often originating on obscure Russian and/or Swedish language websites. The authors also note that some of these forgeries "have utilized fake letterheads and purport to be written by Swedish decision makers, in order to gain credibility and an aura of authenticity".

Overall, while NATO policies have moved in the right direction in a traditional military sense, and while further efforts are needed, political influence operations, whether on political decision-makers or on the broader public, constitute a grave security challenge to the Alliance as well. ■

The views expressed in this article do not necessarily reflect those of the Alliance or its member nations.

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HANNES MÖLLITS

# Russia: reaping the whirlwind in 2017?

Expert article • 2135

Nations continue to struggle for dominance and survival. Usually, the latter is the more important instinct, but in Russia's case they are interlinked - Russia's *derzhava* ('Great Power') instinct continues to drive its actions. The leadership of the world's biggest country by landmass continues to perceive that the country needs to dominate and expand for survival.

Russia has made yet another advance onto the world scene by employing its state (cyber) resources to undermine the foundations of liberal democracy. A series of events – the hacking of DNC and leaking the material through third parties – are of interest in several ways. Firstly, Russian activities are targeted against the foundations of Western power, for its attacks concentrate on how the West legitimises its power. The West is required to fight back in order to survive. Secondly, it also means that Russia is fighting for its survival – in this case, clearly only a mortally wounded bear would attack so desperately. Apparently, the Western way of life is so intimidating to Russia's leaders – perhaps fearing an 'Arab spring' type event in their own country – that an attack on the West was deemed necessary.

The fight for democracy in the West is a fight which West cannot afford to lose. We cannot continue to pursue strategy whereby it would be normal for us to step back and let Russia have a bit more of what we have as we have done so frequently in the recent past. We, the West, will not end up with less and Russia with more, which is what we have been used to accepting for the provisions of peace and prosperity in Europe. Rather, the world order is about to change. Bringing about this change could be a serious miscalculation from the Russian side, since it itself is also going to be affected. Russia has been creating 'controlled chaos' on its periphery throughout its existence. However, this time the chaos might be too large for it to handle.

Domestically, Russia has been known to be much more resilient than any Western nation against a socio-economic downturn. Although the Russian people seem ready to suffer hardship more –

they have not seen 'the good life', in accordance to Western standards – they also have their limits. The Russian economy continues to be structurally weak and it clearly has not become autarkic. This also means that the country needs economic partners. By creating potentially massive amounts of unpredictability and perhaps even instability on its borders, Russia risks losing its Eastern and Western trade partners for good. Russia will continue to suffer from the lack of ports and its only communication shall be thorough already 'stirred up' region of Central Asia. And then there is China.

Coming back to Russia's cyber attacks for a moment – albeit it is difficult to have 'ironclad proof' in the cyber realm since potentially everything could be fabricated, it is sure that the attack on the

The fight for democracy in the West is a fight which West cannot afford to lose. We cannot continue to pursue strategy whereby it would be normal for us to step back and let Russia have a bit more of what we have as we have done so frequently in the recent past.

democracy of the United States (US) was conducted by the Russian government (think of the time it would have taken to plant evidence). The US establishment and private companies have provided ample amounts of evidence to support this claim. 'This brazen attack on American democracy' – as it was described by Senators McCain and Graham – was orchestrated by the

Russian Intelligence Services. It fits into a larger picture of Russian activities in recent years but also historically. It is widely known in the regions that have had to live together or next to Russians that it is part of the 'Russian soul' to go as far as possible and to take as much as possible. If resistance is not met, Russia just continues on that path, be it stealing or attacking.

Let us translate the last thought to activities on Russia's borders. Clearly it has adopted an experimenting doctrine towards conflict generation. It employs a sub-set of its resources in an area, creates conflict and confusion and then leaves it on the 'back-burner'. This releases resources for Russia, but forces other parties to waste resources on solving the mess. The cases of Ukraine, Georgia and Syria have been most notable, but do not form an exhaustive list. To paraphrase the '80-20' approach, Russia will use 20 percent of its available resources to gain 80 percent of the results and the target country has had to put forward 80 to recompose 20 percent.

Therefore, I would argue that the hack against the Democratic

Party in the US is just the first of many to come. Russia has won so many 'points' out of this attack that it is likely to use the same instrument and type of attack again and again. I agree with the aforementioned senators that the price Russia has had to pay is not even close to the perceived benefits it received. Russia experimented in how to generate a favourable environment in the system of its opponent and succeeded. It may soon realise that this tool will work in any democratic nation. It works because in some respects democracies are inherently weak – they are open by nature – the governing bodies need the legitimisation (and checks and balances) from the people to make sound judgments and decisions. We still have representative democracies because that is the only workable solution we have come up with so far.

Accordingly, we will continue to have representatives who will continue to take decisions on our behalf and for themselves. They are bound to be not liked by at least some part of society. It therefore becomes quite easy for an autocratic nation, which is ready to employ all of its resources, to undermine a democratic country. Cyber has just amplified the effects of openness and we have not been able to cope with the downsides as quickly as the attackers have tapped into their potential.

Jumping back to the topic of Russia's survival struggle, the question arises: which Western nation will suffer the first coup attempt staged by Russia and when? Meddling processes with the upcoming French and German elections are already well on the way (cyber attacks also against German deputies, direct financial support for some of the more Russian-leaning parties are well documented).

Of course, in the globalised environment, there is some influence from nation to nation. However, any attempts to go beyond the well-established practice of keeping pressure to a minimum between great powers should not be abandoned lightly. Russia must understand – and that would be the only thing Russia and its autocratic regime will understand – is that this will have implications on its regime as well. So far Russia has been afraid of a 'Russian Spring' happening. By undermining Western democracies it may eventually fulfil its own prophecy. It will create so much instability outside of its borders that the backlash will most likely sweep away the current Russian regime itself. ■

The author writes strictly in his personal capacity.



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# Defending Baltic States: overlooked importance of Saaremaa and Hiiumaa islands

Expert article • 2136

**D**uring the First World War Russia and Germany acknowledged the importance of Saaremaa and Hiiumaa Islands. In October 1917 Russian forces lost control of the island after the Germans launched one of the most daring and largely forgotten joint amphibious operations of the First World War called Operation Albion. William S. Lind summarised the outcome of the operation by saying that the Germans, by taking the control of the islands, sent a powerful message to the Russian government.

Even today, there are three main factors which add operational significance to Saaremaa and Hiiumaa Islands for defending the Baltic Region in the case of conventional war between NATO and Russia. Firstly, control of the islands impacts on freedom of navigation in the Baltic Sea, particularly sea routes in and out of the Gulf of Finland; secondly, the islands are natural barrier enabling control over the entrance of the Gulf of Riga and consequently access to a number of ports, which are critical for service support operations; and finally anti-access capabilities deployed on the islands allow for power projection over a significant portion of the Baltic Sea, as well as the western part of mainland Estonia and Latvia. Certainly, these considerations have to be seen in the much broader context of the Baltic Sea and the security of the whole region.

To put it into Corbett's words: Russia has become only sea power in the Baltic region 'capable to command of the (Baltic) sea or to prevent the enemy from securing it'. Russia continues to grow its maritime capabilities. 75 ships of various types and 2 submarines of the Baltic Fleet are going to be augmented by a newly formed division consisting of five new Buyan-class corvettes, which are the most modern ships in the Russian Navy. The formation of this new corvette division is planned to be completed by 2020. The current capabilities of the Baltic Fleet and anti-access weapon systems and offensive capabilities deployed in Kaliningrad enables Russia to establish control over maritime communication lines; protect Kaliningrad to establish sea control in the Baltic Sea; conduct amphibious operations; destroy air, land and maritime targets in the Baltics, leaving very little space for NATO maritime operations.

Putting these factors into the context of a potential conventional war between NATO and Russia in the Baltic region, if Russian forces took control of the islands, it would allow for the extension of their Anti-Access /Area Denial (A2/AD) capabilities, thus denying and/or significantly delaying NATO maritime and air operations over and at the Baltic Sea, as well as Host Nation Operations by local defence forces. Furthermore, possession of the islands would ease Russian forces to conduct amphibious landings and/or deception operations from the west into the territory of Latvia and Estonia. Lose of the islands would seriously hamper the achievement of NATO operational objectives and would stretch already scarce local defence forces to

protect the cost line of the Gulf of Riga.

Consequently, NATO ought to consider the pre-deployment of Allied forces on the islands to geographically extend NATO's military presence in the region, by extending the alliance's defensive perimeter into the Baltic Sea, thus contributing to the achievement of deterrence effects. A list below illustrates military assets, capabilities and security infrastructure which could be deployed or developed to achieve the desired deterrence effect, and prepare the Baltic States and NATO better for the worst case scenario:

- Mobile sea and air surveillance assets and other sensor systems to establish extended situational awareness, monitor maritime communication lines and enable target acquisition;
- Extension of the capabilities of the existing airfield on Saaremaa Island which would allow deployment of aircraft to the war zone for combat, service support missions and search and rescue tasks in peace and wartime;
- Defensive counter air assets to conduct air surveillance, protect deployed troops, equipment and infrastructure, and set preconditions for establishment of favourable air situation/air superiority;
- Other A2/AD assets, such as anti-ship artillery and missiles;
- Development of the existing naval base to enable logistic operations and maintenance for NATO vessels operating in the region;
- Boosting capabilities to land forces on the islands. The size and composition of the land forces on the island should be based on the task to protect the infrastructure and equipment, and counter airborne and SOF operation.

Such measures would send a very powerful signal to Russia, as well as signify the Baltic States' own self-defence commitments if all three Baltic States together took the initiative in planning and implementing this recommendation. Furthermore, building security infrastructure and deploying military assets on the islands would save resources otherwise needed for coastal defence purposes as well for the development of the naval capabilities required to deny attacking forces. ■



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# Thucydides, Melos and the Åland Islands

Expert article • 2137

Thucydides wrote *The Peloponnesian War* in 431 B.C., in order to describe the conditions prevailing and the choices made that contributed to the war between the city-states of Sparta and of Athens. Thucydides approaches a vast number of issues of relevance still today, including the disintegration of societies as in Corcyra (Corfu), the devastating effects and horror of the ensuing civil war there and the double standards used in the powerful city-state of Athens with regard on the one hand its internal affairs and on the other hand the treatment of 'the others'.

One the more intriguing passages in the book is the dialogue between the representatives of Melos and the Athenians on the possibility for Melos to remain neutral in the war. Indeed, the entire book starts off by a general consideration of the negative effects of taking sides, often very hastily, by the various city-states. Thucydides 'could see the rest of the Hellenic race taking sides in the quarrel', as a quote from the introduction tells us.

Melos was a small island that had remained neutral in the war between Athens and Sparta, whereas they had, in fact, joined forces with the other Greek armies in the Persian wars. The Athenians, explain behind closed doors to the Melians that 'right, as the world goes, is only in question between equals in power, while the strong do what they can and the weak suffer what they must'. The Melians ask the Athenian envoys in this unique dramatized dialogue:

'So that you would not consent to our being neutral, friends instead of enemies, but allies of neither side?' And the answer from powerful and democratic Athens is:

'No; for your hostility cannot so much hurt us as your friendship will be an argument to our subjects of our weakness, and your enmity of our power.'

Whereupon, Athens put Melos under siege and eventually, and only after treachery, concurred the island and put to death all the grown men whom they took, and sold the women and children for slaves, and finally sent out five hundred colonists and inhabited the place themselves.

Thucydides has been looked at, by some, as the father of a realist view of international relations understood as a bipolar struggle for control and power within a zero-sum game. However, Thucydides' work does not seem to endorse such an oversimplified view nor an immoral or anarchic international realm. He dramatized a unique dialogue precisely because this is a uniquely tough situation. The Athenians want the negotiation to take place behind closed doors, thus admitting that their arguments would not hold nor be found acceptable in the ears of a wider audience. The Melians argue on the grounds of forbearance, fairness, decency or equity (*epeikia*), putting these arguments on the same level as those of military might. This is 'the privilege of being allowed in danger to invoke what is fair and right'.

The Melians argue also about complexity, i.e. against an oversimplifying zero-sum bipolarity game. The Melians ask 'how can you avoid making enemies of all existing neutrals who shall look at our case and conclude from it that one day or another you will attack them? And what is this but to make greater the enemies that you have already, and to force others to become so who would otherwise have never thought of it?' and they conclude that 'that the fortune of war is sometimes more impartial than the disproportion of numbers might lead one to suppose'.

Societies and international affairs are indeed constantly fluctuating. While there may be certain constants in the behaviour of empires, cities, states and individuals, the possibilities for interaction,

dialogue, cooperation, reciprocity and conflict are always open. In this case, as has been said, the study of history is only a guide, not a prescription. Indeed, in the very next chapter in the book of Thucydides, we learn that Athenian arrogance had soon thereafter to pay a heavy price in their next

Thucydides has been looked at, by some, as the father of a realist view of international relations understood as a bipolar struggle for control and power within a zero-sum game.

expedition to Sicily.

The demilitarization and neutralization of the Åland Islands, originally established in 1856, and firmly based on international law, is perhaps not so different from the case of Melos. In a strict military realist approach, like the Athenian one, the Åland Islands could be perceived as a provocative anomaly. Any military vacuum should be rectified by the re-introduction of military presence, some would argue. Another way of looking at the matter is that a long-lasting multiparty regime modifies the stakes at risk and forms the behaviour of many actors. A demilitarization regime intends to move a potentially hot spot from the military end of a spectrum of possible alternatives towards the political and diplomatic one. The demilitarization is to be upheld primarily through diplomatic rather than through military means. This is also why some experts describe demilitarization as a confidence-building measure. Is neutrality dead? Yes, would argue the Athenians. No, would answer the Melians. ■

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# Opportunities and challenges of the Baltic Sea Region (BSR) electricity network

Expert article • 2138

One of main Europe's goals is to ensure sustainable, competitive and secure energy market in the Baltic Sea Region (BSR) and in the European Union (EU). In this context, extremely important is higher integration of European energy market and cooperation between electricity transmission system operators.

There are five regional groups based on the synchronous zones: Continental Europe - former UCTE, Nordic - former NORDEL, Baltic - former BALTSO, Great Britain - former UKTSOA and Ireland-Northern Ireland - former UKTSOA. These Regional Groups have a permanent character that ensures continuity in ENTSO-E's system operation activities and allows for realization long-term network development projects. ENTSO-E, the European Network of Transmission System Operators, is an association that represents 42 electricity transmission system operators from 35 countries across Europe. The Ten-Year Network Development Plan (TYNDP) for electricity is one of the ENTSO-E's deliverables in order to build well interconnected and up-to-date electricity infrastructure.

ENTSO-E publishes every even year report on the 10-year network development plan (TYNDP) that presents the scenarios of the electricity transmission grid development in the next 15 years. The TYNDP 2016 foresees up to 150 billion euros of investments in grid infrastructure. Under the ENTSO-E structure six development regions have been distinguished for grid planning and other system development tasks. One of these regions is BSR for which Regional Investment Plan was proposed in 2015 as part of the TYNDP 2016. The Regional Investment Plans, based on past TYNDP and continued on current pan-European network plans, are crucial in European network planning approach and building integrated energy market. The objectives for grid development within BSR are related to both the current trends in the European energy markets and specific characteristics of the region.

In recent years investments led to the end energy isolation of some EU countries. Electricity interconnection LitPol Link between Lithuania and Poland and Nordbalt between Sweden and Lithuania significantly improved integration of energy market in BSR by creation the so-called "Baltic ring". It was also one of priority projects of Baltic Energy Market Integration Plan. Strengthening of interconnections between Baltic countries as well as reinforcement of Baltic countries internal grids are still main corridors both for the Baltic States and the European Union.

Further interconnection of Nordic countries with mainland Europe are considered in the scope of new interconnectors. To achieve the interconnection target for 2030, the levels of interconnection between the Nordics, Baltics and the Continental Europe East should range from 1 GW to 2,5 GW.

Interconnections of Poland with Germany, the Czech Republic and Slovakia also belong to main interconnection challenges in Europe and allow to increase market capacities. The optimal level of capacity exchange, for strengthening the grid in Central Eastern Europe between Germany, Czech Republic, Slovakia and Poland, in 2030 is scheduled to be in the range from 2,5 GW to 4,5 GW.

Another problem is synchronisation and integration of the Baltic States with the European power system, to enhance security of their supply from the West Europe. TYNDP include three scenarios of Baltic integration through:

- the synchronization with the Continental system,
- the synchronization with the Nordic system,
- support by existing HVDC-links.

Latvia and Lithuania aspire to a better integration with the Western European system via Poland, while Estonia via Finland. At present, transmission system operators of the Baltic States (together with Belarus and Russia) form the so-called BRELL energy ring. To decrease dependency on non-ENTSO-E countries, Baltic States have agreed to disconnect their grids from BRELL by 2025.

In order to satisfy raising electricity demand and to ensure security of supply in the Baltic Sea Region and in the whole Europe electricity transmission grid need modernization and expansion, especially in Eastern Europe. Electricity grid development is very important because of the increased deployment of renewable energy. Electricity grids must also connect power stations that generate energy from renewable sources, which significant development is also included in the TYNDP scenarios. EU energy target for 2030 assumes at least 27% in the final energy consumption will come from renewables.

The Connecting Europe Facility (CEF) that is EU funding programme notes, inter alia, the problem of ageing energy infrastructure in Europe. Taking this into account, electricity grid infrastructure development must significantly accelerate. EU's energy infrastructure is not able to cope with growing energy demand in its current state. ■

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# Russia's military aggression and the security threats posed by "purely commercial" projects in the Baltic Sea Region

Expert article • 2139

On 13 December 2016, representatives of two Swedish local authorities received a confidential briefing from the Swedish Defence Minister Peter Hultqvist and Foreign Minister Margot Wallström. They were informed about the security threats associated with the construction of *Nord Stream 2*. Karlshamn in Blekinge and Slite on Gotland had received seemingly lucrative requests that would allow them to play a part in the logistics plans for the construction of *Nord Stream 2* to deliver more Russian gas to Germany. The local decision-makers had been asked to give their consent to the time-limited use of harbour and storage facilities. The Kremlin and the Russian state controlled *Gazprom* have put their full weight behind *Nord Stream 2*. Once constructed, the combined transport capacity of *Nord Stream 1* and *2* will amount to 110bcm, solidifying Russia's grip on German energy supplies.

After the meeting in Stockholm, the representatives of Karlshamn and Gotland explained to the press that they had received information about security threats associated with the gas pipeline project that made it difficult for them to endorse the business deals. Defence Minister Hultqvist told the press that *Nord Stream 2* poses a threat to Sweden's national security, both during the construction period and in the long term. He made reference to Sweden's Royal Navy base in Karlskrona and the F17 Kallinge Royal Airforce base near Ronneby, both located in the proximity of Karlshamn. He also highlighted Gotland's strategic position and the Armed Force's work to establish a permanent military presence on the island, in response to the deteriorating security situation. Due to the classified nature of the information shared with the local authorities, Hultqvist was unable to specify the threats posed to Sweden by *Nord Stream 2*, but insisted that they are tangible and serious. Foreign Minister Wallström added that *Nord Stream 2* has negative consequences for Ukraine and European security and that it contradicts the *Energy Union* objectives with harmful consequences for the EU's energy supply security.

The announcement came as a shock to *Gazprom's* lobby group in Sweden. The supporters of *Nord Stream 2* immediately attacked Swedish decision-makers and alleged that the security concerns were fabricated and that an "irrational fear of all things Russian" was behind the sudden rejection of the *Nord Stream 2* business deals. Others hastened to add that the local harbour and storage facilities would be used by sub-contractors from the Netherlands and Malaysia, trying to shift the focus away from Russia's control and *Gazprom's* ownership of *Nord Stream 2*. The broader ramifications for Sweden's Baltic Sea trade were also brought into the debate. It was alleged that a "No!" to the Kremlin's plans of binding Germany to Russian gas supplies could have negative repercussions for Swedish companies doing business in Russia. The local authorities noted that it was unreasonable that the responsibility for Sweden's national security should rest

on their shoulders. After all, the deal with *Nord Stream 2* promised to be lucrative for their constituency and negotiations had progressed so far that it was politically problematic to back from the deal. The national government had become involved too late, suddenly forcing them to switch from promoting local economic interests to protecting Sweden's national security.

The following week, on 20 December 2016, it was made public that the Swedish government had put a stop to the construction of *Blekinge Offshore*, plans for a major wind energy project in Hanö Bay. The wind park was to consist of between 350 and 700 offshore turbines and could have created 400 new jobs for about ten years. The negative decision came as a shock to the company and to many stakeholders and supporters at the local level in Sölvesborg and Blekinge. The decision was heavily criticized for coming so late in the planning phase, and for undermining strong local business interests. The Swedish government explained its decision to put a stop to *Blekinge Offshore* on the grounds of unacceptable long-term negative consequences that the wind farm would have had on the Swedish Armed Forces and Sweden's national defence capability.

The controversies in Sweden brought to the fore new challenges for decision-makers resulting from the deteriorating security environment. The Russian Armed Forces' aggressive military posturing against EU and NATO member states and Russia's warfare against Ukraine place new demands on national governments. Security in the Baltic Sea region has to be considered from a broader perspective and commercial projects need to be scrutinized more carefully to assess their impact on the Armed Forces and national security. The gap between the local and the national level needs to be closed and communication with local actors must improve to ensure that "business deals" that negatively affect national security are not assessed on their commercial merits alone. Russia's demonstrable offensive military ambitions and capabilities demand that extra attention is paid to business deals endorsed by the Russian state. To prevent the aggravation of existing national defence vulnerabilities vis-à-vis Russia, all riparian states will need to assess the side-effects of *Nord Stream 2* and other on- and offshore as well as subsea projects, to bolster their security and enhance their defence capabilities. ■



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# Additional routes will increase competition in European energy market

Expert article • 2140

**G**azprom is frequently portrayed as the Kremlin's foreign policy arm, but few experts noticed dramatic changes in the company's business strategy in the European Union. Gazprom's pipeline gas supplies to Europe are currently triggering a buying spree by European energy companies. In 2016 the Company sold 180 bcm of gas to Europe and Turkey and Gazprom's gas deliveries set new records in January 2017. Last year, Russian gas prices were comparable to even cheaper than record-low European spot prices. For example, in end of May 2016, Gazprom's gas prices in Germany were as low as \$145 /1000 cubic meters or about 20 % less than NBP spot price in the UK – the most liquid natural gas market in Europe. Data published by the European Commission showed that in the second quarter of 2016 wholesale natural gas prices in the markets dominated by Gazprom's supplies – such as the Slovak Republic (12.18 euro/MWh) – were lower than in the most developed European gas hubs such as TTF (13.19 euro/MWh).

Gazprom is obviously not eager to ask low prices – in January–September 2016 its year-on-year operating profits fell from \$17.6 billion to \$8.31 billion but the company had no choice if it wanted to keep its market share. Russia's gas flagship also showed flexibility in its market approach. In March 2016, Gazprom reached an agreement with Germany's Uniper on price adjustment to its' supply contracts. In December 2016, this Russian gas company specified it was prepared to change its business practices to settle an EU antitrust case initiated by the European Commission. Russian company increased supplies and therefore gained market share by playing by the rules of the market.

When in Rome, do as the Romans do is the new motto of Gazprom. Diversification of supply routes and sources of energy is one of the key goals of Europe's energy policy. In the context of this initiative, EU promoted its' Southern Gas Corridor in order to bring natural gas from the Caspian region to the European markets. In 2016 the European Commission also adopted European liquefied natural gas (LNG) strategy where LNG was presented as an important diversification and security of supply tool. Brussels rightfully expected that competition between traditional suppliers and newcomers will bring additional benefits for the consumers in the region, but suppliers also decided to join Brussels' (diversification) games by proposing their own pipelines such as Nord Stream – 2 and the Turkish Stream. For example, Gazprom's diversification strategy mirrored the EU's own attempts to diversify its supply sources and energy export routes.

These new routes are however not about politics but about economics, supply-demand balance and are based on solid economic calculations. For example, the Nord Stream – 2 pipeline may be an

expensive undertaking from CAPEX perspective, but the project's OPEX will not be so high: the main compressor station in Russia can be fueled by local gas supplied at domestic prices of less than USD 2/MMBtu (including transportation cost from the gas fields in Western Siberia).

Furthermore, Nord Stream 2 supplies will be able to compensate for a falling gas production in Northwest Europe with the regasification terminals in this part of Europe, offering a viable and competitive alternative to pipeline gas supplies. In fact, a bulk of domestic gas supplies in the EU originate from rapidly depleting fields situated in the UK and Netherlands. For instance, natural gas production in the UK declined from 96.4 billion cubic metres (bcm) in 2004 to 39.7 in 2015. During the same period, Dutch gas output fell from 68.5 bcm to 43 bcm. According to the BP Statistical Review of the World Energy, overall indigenous production in Europe (EU plus Norway) has decreased from 299.5 bcm in 2004 to 237.3 bcm in 2015. This number could fall further to 170 bcm in 2035 (CEDIGAZ-2015). Long-Term Outlook for Gas 2035 published by Eurogas estimates European natural gas demand in 2035 between 394 bcm to 527 bcm. Thus, by 2035 the EU will require between 62 bcm/year and 194 bcm/year in additional gas imports. Russian gas – if priced competitively – together with LNG and other pipeline projects will have a role in addressing Europe's growing supply-demand gap. Furthermore, the presence of alternative supplies – in the form of liquefied or pipeline gas fixing a price ceiling – and a well-functioning, competitive EU gas market, will hedge European consumers against high energy prices.

Europe should think out of the box and do not look for a black cat in a dark room, especially if it is not there. The EU should use all reserves and supply routes available to achieve a smooth and cost-efficient transition to the low carbon future. The recipe for the energy security is also quite simple – one should let different infrastructure projects compete with each other for customers and a market share, obviously within the established rules of the game. ■

Disclaimer: the views expressed here are solely those of the author and do not represent views of his organization.



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TOR MORTEN OSMUNDSEN

# The clean fuel opportunity in the Baltic Sea

Expert article • 2141

IMO – the International Maritime Organisation - agreed last year to limit Nitrogen Oxide (NOx) emissions from ships' exhaust gases in the Baltic Sea and North Sea countries for new ships built in or after 2021. It is expected that this decision will enter into force as a larger Nitrogen Emission control area (NECA) in May this year.

This decision supported by the EU strategy for the Baltic Region and recent proposals from the Baltic Marine Environment Protection Commission (HELCOM) and the countries surrounding the North Sea, is a very important one when it comes to a cleaner Baltic Sea but also for the sustainable development of the marine sector in the region.

The effect of the 2015 IMO enforcement of the 0,1% Sulphur (SOx) limit under the SECA has - according to reports from HELCOM - led to 88 % reductions in SOx emissions from shipping in the Baltic Sea region. These positive results must have been an inspiration when IMO last year also decided to reduce global Sox emission limit from 3,5 to 0,5% already from 2020.

Maritime transport has been a catalyst for economic development and prosperity throughout its history. In Europe, maritime transport enables trade and contacts between all European nations and provides the main vehicle for European imports and exports to the rest of the world. Overall, maritime industries are an important source of employment and income for the European economy.

The importance of the maritime transport is certainly the case for the Baltic Sea being one of the most heavily trafficked seas in the world with about 2000 ships in the sea every day and accounting for 15% of the world's cargo transportation.

However, the maritime sector is also a major source of the harmful air pollutants CO<sub>2</sub>, SO<sub>x</sub>, NO<sub>x</sub> and particles with negative impact on the climate, health and marine eco-system. By 2020 shipping emissions of SO<sub>x</sub> and NO<sub>x</sub> could exceed the emissions of these pollutants from all other sources in the EU. It is widely accepted that this pollution must be reduced dramatically to protect health and the environment and to secure shipping as a sustainable form of transport.

So the question that is being asked in the Baltic Sea region as well as globally is how to increase transportation by sea while reducing the environmental impact and securing a healthy maritime business?

One of the solutions is LNG as marine fuel. LNG meets all current and expected SO<sub>x</sub> and NO<sub>x</sub> requirements, eliminates particles and reduces CO<sub>2</sub> by at least 20%. LNG marine fuel is available and economic efficient in the long run. The testimonials from the ship-owners using LNG as fuel are positive.

There is a lot of momentum and collaboration between stakeholders on innovation, sharing and learning on LNG technology, infrastructure and safe and efficient bunkering operations supported by dedicated national and EU funding programs.

In Norway where the first LNG driven ferry was launched in 2000, the NOx Fund established between the Government and the maritime industry sector to reduce NOx emissions has received 950 applicants and about 80 Mill Euro has been granted. The outcomes are about 50 LNG driven vessels and 35000 tons NOx reduction in Norwegian waters and a LNG industry network with 50 + companies.

The Zero Vision Tool (ZVT) program steered by the Swedish and Finnish Shipowners and Port Associations provides a platform for collaboration on finding common, workable and sustainable marine solutions for the Baltic Sea among industry, academy, agencies and administrations. The Pilot LNG and Baltic Soxlution projects (both EU funded) prove the benefits of LNG and support deployment of LNG bunkering infrastructure in the region.

The HELCOM commission has established a shared "Green Technology and Alternative Fuels Roadmap" which provides a forum for a structured dialogue between public and private sector and promotes collaboration with other initiatives at regional and international level.

The Baltic Port organization supports the development of LNG bunkering infrastructure together with EU funding programs. About 15 ports in Finland and Sweden have or are considering a LNG bunkering infrastructure project. Other ports are considering favorable port dues for ships with good eco performance.

LNG import terminals are built in Sweden and Finland to serve the land industry and the maritime sector. Skangas will this summer launch the first LNG bunkering vessels and provide ship-to-ship bunkering services in the North and Baltic Seas. The industry is collaborating on developing standards to secure efficient and safe bunkering operations.

LNG as marine fuel seems to be the answer to reducing the harmful pollution as well as securing the sustainable development of the maritime transport and business in the Baltic Sea. Further, the Baltic Sea together with the Norwegian Sea are already the benchmark and frontrunner for the implementation of LNG as marine fuel. ■

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ESA HÄRMÄLÄ

# The Baltic Sea Rim –Biomass base of Europe

Expert article • 2142

**T**he countries around the Baltic Sea have the biggest forest biomass resources of Europe. These resources are steadily growing as the annual increment exceeds felling. The forest resources of Finland, Sweden and the Baltic States are well known but actually both Germany and Poland are at the same level or above their northern neighbours.

Especially the examples of Finland and Sweden show that a well managed forest is a cake that you can eat and have it too. During the last 100 years felling, annual growth and growing stock in the forests have all grown. The biomass from forests have replaced huge quantities of fossil energy and raw materials and at the same time forests have become much larger carbon sinks than before.

Today there is a lively debate going on of the role of forest biomass in combating climate change. Especially environmental non-governmental organizations (ENGO) are sceptical or even set against the increased use of forest biomass in energy production and to replace fossil raw materials in general. Most of their arguments are not sustainable.

ENGOS warn about burning trees for energy. Well, if we forget firewood for heating of saunas of the summer cottages, which is normally harvested manually from no longer than 100 meters from the sauna, trees are not burnt for energy. Energy from forests is always a residue or waste of forest management (cleared bushes and small diameter trees from thinning and young stands), forest harvesting (bad quality trees, branches and tree canopies) or timber processing (saw dust, chips, black liqueur, bark). Practically no tree in these countries is grown or harvested for energy only.

ENGOS say that when a tree is burnt the carbon is released in seconds but it takes at least 50 years for the tree to sequester the carbon back again. The old saying "seeing forest for the trees" fits here perfectly. Every single day when forests grow more than harvested they are a sink, not an emitter of carbon. This is the case in the Baltic Sea area. There is no carbon debt appearing. Forest biomass is truly carbon neutral.

ENGOS warn that increased use of forest biomass is a threat to biodiversity of forests. On purpose they forget that sustainability of forestry is not decided by the use of the energy component of trees (the above mentioned residues and waste) but how trees were grown and harvested. It's a matter of sustainability of forestry, not sustainability of energy from forests. In sustainability of forestry the countries around the Baltic Sea are no doubt world leaders.

Especially forest certification schemes (PEFC, FSC) have clearly improved the situation. A recent independent study concluded that in Finland the PEFC certification, which covers close to 90% of Finnish forests, has been a major contributor in maintaining biodiversity. From the biodiversity point of view Finnish forests are much better off than some of the country's other important ecosystems, like coastal waters, wetlands and alpine habitats.

ENGOS also forget the fact that it's always better to use carbon that already is rotating between vegetation and the atmosphere instead of digging fossil carbon and releasing it to the atmosphere. It does not change the big picture even when one uses some fossil energy for timber harvesting and transport.

According to EU's own estimations biomass will during many decades be by far the biggest new source of renewable energy leaving for example wind and solar clearly behind. The countries around the Baltic Sea are well placed in this development. This is not only because of a good sustainable raw material basis. These countries have as a consequence

of long traditions in silviculture well managed forestry. They also have competitive forest industries which have a central role in mobilizing timber sales, harvesting, transport and processing. Above all, these countries have integrated value chains based on forests including research and development. Energy use is only the first step on the way to a post-fossil era. There are growing expectations to replace fossil raw materials by renewable wood for example in construction and chemical industries. ■

ENGOS also forget the fact that it's always better to use carbon that already is rotating between vegetation and the atmosphere instead of digging fossil carbon and releasing it to the atmosphere.



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EDWIN BACON

# Russia's parliament and the potential for political evolution

Expert article • 2143

For most observers, all significant developments in relation to Russian politics in recent months and years have taken place in the international sphere. This is what grabs the headlines as most significant. Should attention turn to Russian domestic affairs, then it is this same international angle which is to the fore – the effect of US and EU sanctions on the Russian economy, or the human rights cases that are so often couched in terms of Western influence and ‘fifth columnists’.

But what about Russia's domestic politics? The sense for the intelligent observer who takes an interest in Russia but does not follow it closely is of a largely impregnable authoritarian regime maintaining power. Its supporters call this stability, its detractors prefer the term stagnation. The broad picture of democratically deficient continuity in Russia's domestic politics is accurate. Within the frame of this picture, however, changes do occur. The parliamentary election of September 2016 exemplifies.

On the one hand, the basic facts remain the same. The pro-regime party, United Russia, won the vast majority of seats in a flawed electoral process, including gaining 96% of the vote in Chechnya. The second and third parties – the Communists and the Liberal Democrats respectively – are still led by the same people who were at their helm during the first post-Soviet Russian election in 1993, Gennady Zyuganov and Vladimir Zhirinovskiy. Continuity could even be seen in what might seem at first glance to be variation, with yet another amendment to the electoral process bringing to mind the old maxim that ‘constant change is here to stay’. The replacement of an entirely proportional electoral system with one in which half of the parliament's seats are filled under a majoritarian constituency-based vote simply represented the reintroduction of the system abandoned in 2007.

On the other hand, a major shift occurred with regard to the representatives elected. Half of the deputies in the Russian parliament of September 2016 are new to the Duma. The significance of this remarkable turnover in the make up of the parliament is enhanced by the fact that the Putin regime has embarked on a process of cadre renewal recently. Old hands such as Sergei Ivanov and Vladimir Yakunin have been moved on. Newer figures, such as Head of the Presidential Administration Anton Vaino, have moved in, prompting talk that Putin sees his eventual successor as coming from the generation of younger loyal followers who have built their career in recent years and are acclimatised to Putinism. That being the case, the new cohort of parliamentary deputies offers a potential pool in which to fish for the leaders of tomorrow, especially since 60% of United Russia deputies are new to national level politics.

The idea that a renewal of cadres is underway within Russia's ruling regime has some traction, but it requires two caveats for now. First, just because there are 204 new United Russia deputies in parliament, this does not mean that they are all young upwardly mobile political figures. More than half of them are aged 50 or above, and the cohort as a whole does not look particularly different or vibrant. Only 14 % of United Russia's deputies are women. Nevertheless, there remains a fairly sizeable group of over 80 United Russia deputies in their 30s or 40s who might fit the mould of loyal, business-minded, and administratively competent figures from across Russia without any particular background in capital city machinations or the security services. Out of this group expect to see some of Russia's future ruling élite emerge.

The second caveat concerns the role of the Duma in Russian politics. Will this influx of new deputies, most of whom are sent to parliament from a specific constituency, increase challenges to the executive from the legislature? If the first hundred days of Russia's new parliament are anything to go by, the prospects are not yet good. The Duma has continued to be a conduit for government measures to pass through with too little challenge, and of the 120 draft bills discussed in the opening months of this Parliament,

almost two thirds were initiated by the government. The new speaker of parliament, Vyacheslav Volodin, comes directly from the presidential administration. Although his position ought to be one of organiser-in-chief rather than boss, his main efforts since the election have been directed towards creating a more disciplined parliament with less absenteeism.

United Russia deputies are well aware that such an approach means that they must show compliance or lose privileges. The Putin system has not allowed a parliament that matches its constitutional role of keeping in check the power of the executive on behalf of the people. It has operated instead like another branch of government. ■

Continuity could even be seen in what might seem at first glance to be variation, with yet another amendment to the electoral process bringing to mind the old maxim that ‘constant change is here to stay’.



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# More and better investment in the labour market integration of refugees

Expert article • 2144

In light of the sharp rise in the number of refugees, their better and faster integration in the labour market is now considered a central challenge in EU countries – including those nations that tend to take a sceptical stance on the admission of refugees. While the Scandinavian countries, in particular, already have years of experience in the labour market integration of refugees, other countries are now increasingly establishing refugee support programmes. However, most countries have only just begun implementing effective integration strategies.

These are the central findings of an international study “From Refugees to Workers” commissioned by the Bertelsmann Stiftung that compared strategies and measures for the labour market integration of refugees in nine European nations. In addition to state integration policies, the research team from the Migration Policy Centre at the European University Institute in Florence also examined municipal and non-profit integration projects for the study.

The survey shows that, in the past year, almost all of the countries studied have launched new programmes or broadened existing assistance measures to additionally benefit refugees. In total, the study counted 94 programs of different kinds in the nine countries. Language and orientation courses, measures for the assessment of occupational qualifications, and placement and counselling services are especially widespread. In some cases, the corresponding budgetary resources have also been substantially increased.

## Many pilot projects, few wide-scale offerings

However, none of the countries is currently dedicating sufficient resources to meet the increased need for language courses and assistance measures. Many of the measures identified are merely pilot projects, with correspondingly low numbers of participants. Personnel shortages and uncertainties with regard to financing lead to long waiting periods and impede access to the available places.

Refugees in the United Kingdom and France receive the least support. These two countries lack a state-organised integration policy, leaving refugees dependent primarily on projects run by non-profit groups.

In contrast to this, Denmark and Sweden have taken the most ambitious approach. Both countries define integration as an area of public responsibility, and both offer all refugees and their families multi-year introduction programmes that combine language instruction, vocational orientation, internships and subsidised employment opportunities. Due to the high numbers of refugees, Denmark and Sweden currently face the challenge of further expanding these cost-intensive programmes.

## Administrative hurdles too often hinder employment

Despite the differing framework conditions, similar challenges confront the various countries. These include the development of measures that take into account refugees’ special needs for assistance. Most of the countries studied responded to the new situation by expanding existing support offerings for immigrants to include refugees as well. It

is well known, however, that people who have immigrated as refugees have significantly greater difficulty finding employment than do other immigrants. This must be taken into consideration in designing assistance measures.

There is an additional need for improvement in the coordination of the employment offices, the municipalities responsible for accommodating refugees, non-profit initiatives and the many other parties involved. The development of a coherent overall strategy is urgently needed.

Finally, numerous administrative and legal barriers unnecessarily complicate the job search for refugees. In many cases, asylum seekers who are not yet recognised are permitted to take a job only when no qualified native candidate is available. They are often also not allowed to pursue work on a self-employed basis. The job search is made yet more difficult by residency-related limitations. All too often, legally recognised refugees are assigned to municipalities according to the availability of housing and integration courses, but not the need for labour, thus disadvantaging refugees who are placed in economically underdeveloped regions.

## Early entry and flexible programmes

One of the most important success factors, the study concludes, is allowing refugees to acquire work experience in the receiving country as early as possible. For example, Scandinavia’s experience shows that, in addition to learning the national language, refugees benefit most from internships and publicly subsidised entry-level jobs in the private sector. By contrast, even the best-intended assistance measures help little when they keep refugees in the classroom and away from the labour market. Thus flexible programmes are called for that link career entry with language courses and opportunities for participants to upgrade their qualifications at the same time.

Reliable knowledge about the effect of specific measures remains scarce, however, as up to now little data or empirical studies exist on the labour market integration of refugees. To improve refugees’ job prospects over the long term, EU countries must not only invest more in integration but, in addition, more closely examine the effectiveness of these investments. ■



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# Information warfare – a Hobbesian concept of war in the post-truth era

Expert article • 2145

“The war of all against all” (*Bellum omnium contra omnes*), is a concept of perpetual war, which was introduced by English philosopher Thomas Hobbes in his 17th century books “De Cive” and “Leviathan”. Hobbes realised that, before the emergence of human society, there was a mere war instead. Hobbes did not see the war in purely military terms but as a form of societal relationship. For Hobbes, the world lives in a state of constant anarchy and unregulated relations between actors. The Hobbesian concept of perpetual war was, in many ways, born again in the 21st century, referring to the era which is often called the “post-truth world”. Evidence for it can be seen in Syria, Ukraine and many other places around the world, without any considerable effort made by the international society bringing peace closer. According to the Oxford Dictionary, “post-truth” describes the situation “relating to or denoting circumstances in which objective facts are less influential in shaping public opinion than appeals to emotion and personal belief.”<sup>1</sup> Multiple agent may conduct warfare in different environments, the Internet and social media being among the most influential of them. Contemporary conflict does not only involve actual fighting in military fronts, but also includes the significant increase of the role of information warfare, which takes place in the minds of human beings, by using emotions and beliefs as weapons. Future war may appear as a war of narratives, supported by a limited number of military-related special operations, which could strengthen images of fear and hatred.

Information warfare is able to reshape modern military strategies. Moreover, while the traditional understanding of warfare presumes that information campaigns play merely a supportive role to fighting between military formations, recent conflicts indicate that military operations, more often, rather, support a massive information warfare campaign, which aims to influence human consciousness. George Orwell, in his dystopian novel “1984”, describes a perpetual war, which was fought somewhere far away, and where the only information citizens received was information about victorious battles in unseen military fronts.

*“Attention! Your attention, please! A newsflash has this moment arrived from the Malabar front. Our forces in South India have won a glorious victory. I am authorised to say that the action we are now reporting may well bring the war within measurable distance of its end.”<sup>2</sup>*

<sup>1</sup> English Oxford Living Dictionaries. <https://en.oxforddictionaries.com/definition/post-truth> (04.01.2017).

<sup>2</sup> George Orwell (1949), „1984“, New York and Scarborough: New American Library, p. 25.

The preceding segment may easily fit into any suitable description of information campaigns related to contemporary conflict, where fictional newsflashes are coming to be an irreversible part of political battles, as we see on the basis of the latest US presidential elections, the Brexit referendum in the United Kingdom and, most forcefully, during the migration crisis in Europe.

Russia has been among the pioneers of contemporary information warfare and actively started to use different forms of information campaigns on behalf of its political goals. Russia’s military mind-set started to accommodate to the requirements of the post-truth era and to revitalise the Hobbesian concept of war, where military fighting is just one phase of perpetual war, one battle in the larger agenda of political struggle between powers, necessitated by their self-defined national interests. The annexation of Crimea was a successfully completed non-linear attack, against which the Ukrainian armed forces were not prepared and surrendered without resistance. The war in Donbass presents a different strategy, where a never-ending perpetual war might be the end in itself, in which Russia seems to be more interested in destabilisation of the post-Soviet space, which Russia often denotes as its particular “sphere of influence”.

In his speech, on 26 January 2013, addressed to the members of the Russian Academy of Military Sciences, a Chief of the General Staff of the Russian Federation, General Valery Gerasimow, presented a so-called non-linear approach to military strategy. According to the non-linear strategy, differences between peacetime and wartime will disappear, war is never declared, and military actions carried by uniformed personnel and undercover activities will simultaneously support each other. This approach is close to the concept of hybrid warfare, which was promoted by U.S military strategists in the early 2000s and was initially used to describe the strategy used by the Hezbollah in the 2006 Lebanon War. Consequently, the concept of hybrid warfare started to appear in the discussions about future warfare, to the point where it has finally been adopted and promoted by military leaderships as a basis for modern military strategies. ■

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# Novosti Yle – Finnish news in Russian

Expert article • 2146

**Y**le started broadcasting Russian language radio programmes in October 1990, when Finland's neighboring country was the Soviet Union. At the time the Russian speaking community in Finland was fairly small and the shortwave broadcasts were mainly targeted abroad, where they were followed by Russian speakers all around the World. Letters arrived from readers around the globe.

Yle's Russian radio news was different from most of the Western Russian radio stations since Yle was mainly focused on Finland. International politics was not covered.

By the 21st century shortwave radio broadcasts lost their significance as audiences moved online. Information became more accessible than it had ever been. Yle also gave up shortwave broadcasts, but the Russian service was there to stay. Since the beginning of the 1990's tens of thousands Russian speakers had moved to Finland. The news took a new approach, focusing on local listeners who called Finland their home. By 2010 the main media outlets were our website and television. Yle started television news broadcasts in Russian in May 2013.

The focus of the Russian news, Novosti Yle, is still on Finland's current events, public discussion and providing background information for the target audience. Topics that affect the life of Russian speakers living in Finland or possibly originate from the Russian community are very important. Due to limited resources not all great ideas and material end up online or on the airwaves. The five minute news programme is broadcast every day on television and our website and social media channels are updated regularly throughout the day. The television news bulletins have Finnish subtitles, so that the Finnish speaking audience can understand the topics that are interesting for the Russian speaking community in Finland.

According to Statistics Finland there were 72 000 native Russian speakers living in Finland in the end of 2015, with the prospect of the number reaching 250 000 in the future. I believe that as long as there are no institutions like schools for the Russian speakers to maintain their language the second and third generation will eventually change their language into Finnish or Swedish, but being Russian will still play an important role in their identity. This has happened with the first wave of emigrants and to the Finns that moved to Sweden.

According to studies, Finland's Russians' media usage is divided. A portion of them only follow Russian media, some only Finnish media and the rest follow both. The tone and content of the Russian channels and news have a clear difference to the Western news. Researcher Olga Davydova-Minguet from The University of Eastern Finland wrote in the book "Russian speakers in Finland" published by the Institute of Migration, that "news shows the public carefully selected events and characters, that are circulated by "properly" valuated comments".

Novosti Yle is a part of the Finnish public service broadcasting company Yle and aims to follow Yle's values, independence, reliability and appreciation for people. We're not trying to propagate Finland's positions, but different points of views of Finnish people, Russian speakers etc.

The war in Ukraine was a sort of a watershed even in Finland's Russian news and media usage. Interest in the news increased and the discussion became heated. Russian speakers living Finland had extremely divided opinions which even broke bonds between relatives and family members. Novosti Yle got more feedback on covering the Ukraine crisis than on any other news topic received. A great part of the feedback is posted on the Facebook page of Novosti Yle, where Russian speakers discuss matters related to the topic. Feedback is also received via email, where we receive links to the "true news", but Novosti Yle has never faced real pressure.

Also the Russian media follows Yle Novosti. Before the internet took over, our newsroom received calls whenever something dramatic happened in Finland. These days in the nearby regions in Saint Petersburg and the Baltics Russian language media quotes Yle on a daily basis, from small events to big political and economics news. More significant news is cited by bigger media.

Online byproducts, such as trolling and purposely spreading fake news have greatly increased. From time to time fake news about Finland spreads in Russia. The most well-known cases are custody battles and cases where children of Russian mothers have been taken into custody. Novosti Yle aspires to react to these cases by publishing to the point articles for example on Finnish childcare. We might report about the case and the media attention it got but unlike the Russian media we never publish private people's names in such cases.

Our main target audience is Russian speaking people living in Finland. By giving our multifaceted reporting on issues in Finland and what is happening over here, we hope to empower them to take their lives into their own hands within Finnish society. ■

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OLGA DAVYDOVA-MINGUET

# Finland's Russian speakers as media users

Expert article • 2147

In Finland, Russian-speakers form the largest group of immigrants. At the end of 2015 there were 72 436 people who considered Russian to be their native language. (Statistics Finland 2016).

The research project [Finland's Russian-speakers as media users](#) was funded by the Prime Minister office and was implemented in 2015-2016. It aimed to depict media landscape of Russian-speakers, specify their media use patterns and analyze transnational media influence. A subtext of the project is the widely held concern that EU's Russian-speakers remain in the sphere of influence of official Russian propaganda. Russian television, almost fully controlled by the state, is commonly seen as the main vehicle of producing the present-day so called Russian (tele)nation.

Our research based on interviews of 25 Russian-speaking media users, 8 media experts, and analyzes the ways "the truth" is produced on Russian TV. It revealed the multilayered and complicated involvement of Russian-speakers with the media. Their media use is conditioned by multiple factors. These include their cultural and social capital, age, gender, migration history, ethnic background etc. The Ukrainian 'Revolution of Dignity', annexation of Crimea and beginning of war in the Eastern Ukraine affected the media use of Russian-speakers. These events were extensively presented in national Russian and Finnish media from the opposite juxtaposed positions. Russian-speakers felt their situation as very tense and likewise felt pressed to choose a side.

The transformation from traditional broadcasting and print technologies towards mobile technologies affects all spheres of the media: production, contents and use. The Russian television and internet (Runet) are easily available in Finland. This allows many Russian-speakers to continue ritualistic viewing of Russian TV as they used to do in Russia. At the same time, this enables others to choose programs/content providers and to switch from official state-controlled channels to more independent ones. Internet-based and mobile technologies also allow for more instrumental use of media and combination of different sources of information. These include Russian official news outlets, independent media, international media as well as Finnish domestic media. These established media sources are often combined with the use of social media, which in its turn for some users guides their media use. We have grouped media use of Russian-speakers into four ideal types: ritualistic TV-viewers, politicized TV-viewers, critical media users and those who distance themselves from the media. The ritualistic TV-viewers use mostly entertainment content of Russian and Finnish TV. Politicized TV-viewers usually use Russian TV as a main source of information and keep it truthful and emotionally engaging. Critical media users combine different sources of information and form their own opinion on the basis of different viewpoints. Some people are irritated by the (news) media and try to exclude them from their everyday.

The Russian-language media produced in Finland, so called ethnic media forms a relatively small segment of overall Russian-

speakers' media use. The Finnish Russian-language media, though quite diverse, are assessed as thin and insufficient. The timing of broadcasting of 5 minutes long news in Russian on the public service broadcasting company YLE's Channel 1 is reported as poor, and the news is experienced by users as "too translated" from Finnish instead of being produced "by the Russian-speakers for the Russian-speakers". The main content which YLE produces in Russian is placed on the Internet, and although the critique towards it is the same (that it is "too translated"), it is used by those who follow Finnish events on the social media. The print media suffers from drop of Russian tourism to Finland and as a consequence, drop in revenues from advertising. Finnish "traditional" media in Russian has a double orientation: towards Russian immigrants and tourists, and thus is not felt as completely "ours" and engaging. Instead, the internet-based activities (discussion forums, blogging and videoblogging, social media) are experienced as the media produced "by us and for us", but is less respected than the traditional media. In addition, the internet-based media provide an easy ground for advancing official Russian views and values.

It is obvious, that media production and consumption will remain transnational, and Russian state controlled media will continue to influence on Russian-speaking populations outside Russia. The politics of integration and promotion of multiculturalism in the European countries should take transnational media challenges seriously. Russian-speakers should be taken into consideration as media users and producers, when decisions on public broadcasting, journalists training, media funding are conducted. ■

Full report: <http://tietokayttoon.fi/julkaisu?pubid=14701>



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TEEMU OIVO

# The use of quantity as a competitive edge in Russian TV

Expert article • 2148

Russian state television not only has a hegemonic position in Russia, it is also a relatively accessible and popular information medium among Russian-speakers around the globe. With the current international tensions, the possibilities to use transnational digital age media for manipulating public opinion and undermining social capital have raised concerns in many countries. In respect of this issue, the Finnish Prime Minister's Office financed a research project of a group from the University of Eastern Finland, *Russian-speakers as media users in Finland*, the full report (Fin) of which is now published in tietokaytoon.fi. My part of the research examined how, from their side, the major Russian TV channels (news programmes and talk shows) attracted and addressed their audience over the contested case of the MH17 plane crash in Ukraine in July 2014. One of these ways appeared to be the *large quantity of content*.

When reporting internationally controversial events, reporters of Russian national TV often discuss the narratives of Western media that conflict with their own pro-Kremlin point of view. They profile themselves as alternative media against the hegemonic Western mainstream, a narrative that can address the Russophone TV audience outside Russia that does not relate to nationally domesticated media narratives in their country of residence. While Russian TV is referred to as a smaller media source juxtaposed to the Western or American mainstream, it often has greater resources than national channels in many more linguistically limited media markets with bilingual Russophone audiences. In 2014, for example, the length of daily news broadcasts on the three biggest TV channels of Russia were 3.5 hours (Rossia-1), 2.5 hours (Channel One) and a modest 2 hours (NTV), the latter of which equalled Finnish Ch. Yle1, with most TV news air time in Finland.

Generally, the large quantity of TV air time and production resources enable many ways to attract and persuade news viewers. Rich resources help news programmes to be on the cutting edge in updating ongoing events, present more background to a story, graphics, perspectives, speeches, interviews, details, archive material and connect events with causes and consequences as a continuation of a bigger picture. Extra minutes also add time to repeat previously stated important information that a random viewer might have missed. While not guaranteeing good journalistic quality per se, these quantitative attributes can make Russian TV reporting appear more thorough and trustworthy than the opposing reports with less resources. The lack of point of views in Western news particularly has been criticized by Russian journalists. For disinformation purposes, presenting numerous, various and confusing theories, can distract the viewer from inconsistencies in the journalist's own statements and marginalise non-preferred opposition statements. Moreover, they can distract deliberation or passivate people by insinuating that the truth is unreachable.

It is easier to tell a good news story in 10 minutes than in one. Compelling story-telling is an important way by which Russian TV has attracted transnational attention, whereas critique against the lack of it in the Finnish TV was expressed among our project interviews. When a narrative is intriguing enough, like the conspiracy theory that the shooters of MH17 confused it with the Putin's plane, it catches people's attention and interest to follow and pass it on even without agreeing with its message. The dramatised format fits well to emotional media consumption and supports sentimentally grounded perceptions that are persistent even when faced with valid contradictory information. Indirect and subtle information influence relies also on feelings of familiarity and the viewer's own realisation. In the MH17 reports, for example, discussion about the people responsible was rather suggestive presenting evidence and historical 'precedents', leaving the final (correct) conclusion for the viewer to make. The used narratives benefit from people's tendency to believe in stories matching their own memories, stereotypes, first impressions, fears, hopes and overall views of the world. The wider these frames are shared with audience, the better the message resonates in public discussion and opinion. Hence, to better address Russophone audiences (and generally 'hybrid identities') abroad, media should consider possibilities to format their messages more inter-culturally.

Responding to harmful transnational information influence is a difficult task. While outright false information can be debunked relatively quickly, countering more complicated and confusingly reality-based disinformation requires long-term social measures. In disinformation, real problems and injustices are used with the purpose to distract productive discussion and decision-making. Debunking each false story demands time, one of the scarce resources of journalists and politicians, but conscious public can contribute. For this, and for countering disinformation as well, ensuring good public media literacy is required. ■



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# Union of the Baltic Cities – communicating for a sustainable, smart and safe Baltic Sea Region

Expert article • 2149

On 19–20 September 1991, the Union of the Baltic Cities (UBC) held its founding conference in Gdańsk. Since then, the organisation has become one of the leading networks of cities in the Baltic Sea Region with around 100 member cities. UBC is a voluntary, proactive network fostering cooperation and exchange of experiences between cities to advance and deliver sustainable urban solutions and quality of life, and to promote cities as drivers for smart, green and resource-efficient growth. The UBC and its member cities work in close cooperation with other partners and participate actively in the implementation of regional strategies, notably the European Union Strategy for the Baltic Sea Region.

During 25 years a great deal has changed in the world and the Baltic Sea Region, yet likewise many of the founding principles of the UBC have remained current. In today's world the question is how organisations such as the UBC are able to advance the cities' interests, to influence and communicate in an increasingly polarised and heterogeneous political environment. Despite the current situation, Baltic Sea countries are still in many ways connected by – in addition to the sea – common values and challenges as well as interest and know-how e.g. in matters of sustainability.

During UBC and Land Brandenburg's seminar in the last Strategy Forum of the European Strategy for the Baltic Sea Region, academic experts stated that city partnerships can provide good ground for reconciliation in difficult political situations. Working together on both city and regional levels and sharing know-how promotes the success of all actors in the region, across borders and networks. As 25 years ago, today it is equally if not even more important to build bridges between nations and regions and to find common ground. Cooperation between cities and municipalities has tremendous potential in peace consolidation – but the work needs to be made visible and results accessible to all if we are to have especially governments understand the value of local and regional participation.

One way of actualising this is to develop the ways in which we communicate, interact and cooperate digitally. Essentially, communication is a set of tools which needs to be constantly updated if the organisation wishes to stay current and achieve its goals. City networks

in the Baltic Sea Region face the same practical issues: how can we serve our members better, regenerate and adapt to the changes brought by digitalisation. The best way is to dive in and experiment, particularly in social media. One of the trends in communications are the so called employee or stakeholder ambassadors: the success of an organisation in delivering its brand messages is largely due to active participation of its members and stakeholders who share the organisation's accomplishments and messages in their own personal channels, especially in social media.

In addition to digitalisation and social media, other trends in communications include the increasing importance of emotional and visual content, especially videos, and less formal communications even in the traditionally conservative expert organisations. To achieve their goals, organisations and their leaders can no longer afford to only provide information; instead they need to be responsible, trustworthy

and in genuine dialogue with their audiences. A key success factor is to understand the importance of modern and timely communications as a cross-sectoral and essential tool in all that the organisation does, not as an isolated segment.

One of the central goals of the UBC in recent years has been to energize and streamline its work by forming new UBC commis-

sions and renewing communications. As a part of this, a new website [www.ubc.net](http://www.ubc.net), a renewed Baltic Cities Bulletin and a new UBC logo were introduced in 2016. Before this in 2015, UBC Communications Network consisting of UBC cities' communications specialists was established, with the aim to share best practices and tools and provide a network for consultation and cooperation. In addition to the logo, the entire visual appearance of the UBC went through a transformation into a more modern form. This signified an extensive process of evaluating our goals and values – what kind of an organization the UBC wishes to be portrayed as.

The method in the renewal process has been agile development: developing communications gradually together with the member cities, starting with a beta version and – hopefully – ending up with communications tools that match or even exceed the member cities' expectations. Instead of assuming what the member cities want and need, we involve them in the development process as experts and

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partners through seminars, workshops, surveys and questionnaires. The end product, such as a website, is therefore developed together with the target audiences and according to the feedback received prior and after the launching of the website. Why have we opted for this regeneration process instead of holding on to the methods and channels that have worked for us in the past? Because routines and traditions, as valuable as they are, are not enough. Going forward requires taking chances and moving out of the comfort zone.

The main focuses for the UBC in the next years are implementing UBC Sustainability Action Programme 2016–2021 and EUSBSR and Blue Growth strategies, working towards a new urban agenda for cities, and promoting digitalization and smart growth. Tackling youth marginalization is a very concrete project, demonstrated in the work of UBC's Task Force on Youth Employment and Well-Being which published its report 'The good, the bad and the next practices' in 2015. The results of the Task Force work are available to all and can be implemented throughout the region. Furthermore, the UBC works to solve other current challenges affecting the Baltic Sea Region, such as the flow of refugees. In March 2016, the UBC organised a

conference 'The Impact of the European Refugees Crisis in Baltic Cities'. Implementation of the conference results continues with the main focus on promoting exchange of know-how and practical solutions between the UBC member cities on refugee issues.

In short, UBC continues to further the interests of the Baltic Sea Region and to advance cities as inclusive, diverse, creative, democratic and safe hubs, where active citizenship, gender equality, open communication and participatory policy making are promoted. ■



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# BALTIC RIM ECONOMIES

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IVAN TIMOFEEV

# Security developments in the Baltic Sea Region<sup>1</sup>

Expert article • 2150

**A**fter the Ukraine crisis, the Baltic turned into a most vulnerable point for escalation due to a number of factors that correlate with the common Russia-NATO framework after 2014.

Factor number one is the overall uncertainty about Russia's further intentions. Brussels and other Western capitals are serious about scenarios of hybrid and open military actions against Baltic States. Their argumentation is often far-fetched and inconsequential, bringing Moscow to a loss. The freakiest include the restoration of historic justice by capturing Narva (a sort of repeat of Crimea) or landing on the Gotland Island, with the Swedes already preparing to repel this aggression. However, due to the misunderstanding of Russia's general strategy or its perception as intentionally anti-Western, even these bizarre grounds have drawn a wide response, especially as Russia has been long perceiving NATO's actions there as potentially hostile. At the same time, the Baltic states of NATO are well known as lobbyists for containing Moscow. No wonder, the post-communist countries of the region demand from the alliance a demonstration of readiness for their defense if things get worse. No wonder, real steps to contain Russia have been made in the Baltic. This uncertainty is intensified by differences in the institutional structure of Russia and NATO, as the former is a sovereign state and the latter – an international institution, which generates differences in the promptness in taking decisions and in institutional inertia.

Factor number two relates to the strategic decisions of the two sides for building up their regional potential. Quantity-wise, they should be hardly exaggerated, as the three NATO battalions can hardly change the regional balance of forces. The same goes for deploying the Iskander missiles in Kaliningrad area, which are normally used to scare the EU public. In essence, these moves are minimalist and symbolic. However, their qualitative role is high. NATO has taken concrete steps to contain a possible threat and displayed the bloc-wide solidarity. The battalions are multinational, so any action against them would mean aggression against the entire alliance. For its part, Russia also demonstrates a determination to counter both

NATO reinforcements and possible BMD threats. Due to a high degree of uncertainty, even such small steps may have disproportionately high repercussions, which are of course specific to various airspace incidents. Moscow is irritated by American reconnaissance flights along Russian borders, some of them with shut down transponders. The interception of such flights traditionally gives rise to biased criticism in the West. But in some cases Western grudges are quite grounded, as it this relates to Russian military aircraft flying over NATO ships or airliners.

Factor number three concerns regional geography, primarily direct border contacts between Russia and NATO members. Of particular significance is the spatial compactness, which raises the probability of unintentional air incidents. And of course, it is concerns the detachedness of the Russian territory, as Kaliningrad Oblast is isolated from the rest of Russia and surrounded by NATO members.

Naturally, Moscow is worried. Until now, Moscow showed restraint about the militarization of Kaliningrad but under the current conditions a buildup is very likely. Note that the sides tend to suspect each other of possible unexpected military activities around Kaliningrad.

Factor number four is the presence of two neutral states that could act as game changers. Theoretically, the neutrality of Sweden and Finland could promote stabilization of the region, with

Theoretically, the neutrality of Sweden and Finland could promote stabilization of the region, with Helsinki working as a mediator between Moscow and Brussels on the basis of its experience and prestige.

Helsinki working as a mediator between Moscow and Brussels on the basis of its experience and prestige. But in practice both tend towards a close partnership with NATO. At the extreme, they have discussed joining the bloc, with the trend gaining ground at the backdrop of the Ukraine crisis. In the current environment, the rapprochement of Sweden and Finland with NATO appears irreversible. The question is how far it will go and how Moscow will respond. Either way, these developments should deepen the regional security dilemma, with the least evil outcome being their close partnership with NATO in the absence of formal membership.

Factor number five lies in the lack of progress in settling the Ukraine problem and the aggravation of other differences. The Ukraine controversy provides the long-term negative grounds within the Russia-NATO relationship, with things likely to get worse. Differences with the U.S.A. on Syria and other matters also solidify the downbeat background for the Baltic. In a nutshell, there seems to be a *systemic paradox*, with the cause of the Baltic trouble lying beyond the region that at the same time is gathering a potential for power play.

<sup>1</sup> This analysis is a part of wider piece, issued by Latvian Institute of International Affairs. See Timofeev, Ivan. Russia and NATO in the Baltic. // The Baltic Sea Region: Hard and Soft Security Reconsidered. Edited by Maris Andzans and Ilvija Bruge. Riga: Latvian Institute of International Affairs, 2016.

To this end, the Baltic scenarios may take the following routes.

**Scenario 1.** Sustained containment, with the security dilemma preserved. The sides rely on mutual containment and minimal dialogue. Marine and airspace incidents are highlighted by the media but fail to cause a military escalation even if accidents occur. The buildup of potential is symbolic, as the sides prefer to save their resources. The negative backdrop in Russia-NATO relations holds, among other things due to the lack of progress over Donbas. The sides use containment for domestic and political mobilization. The Post-communist NATO states win, with the political clout rising and the real military threat low. Finland and Sweden drift toward NATO but stay out. As before, Russia does not make the region a priority for military construction.

**Scenario 2.** Inconsistent containment. The security dilemma intensifies, with the external environment deteriorating: the Minsk process is deadlocked and military action in Donbas resumes. Antagonism on Syria grows. A series of incidents at sea and in the airspace gives rise to drastic weapons buildup to be taken up by the other side. Russia prioritizes the region for military concentration. Finland and Sweden accelerate rapprochement with NATO. The region becomes an arena for a local political crisis, although communication channels remain.

**Scenario 3.** Regional conflict. One of the sides ups the ante in order to receive concessions from the opponent. One of them regards the move as a way to solve other problems. Either side is able to take this line of action. The region plunges into a conflict situation. However, the opposing side does not yield and openly counteracts to generate a brief conflict that ends in a draw. The relations rise to a new level of hostility, with the dialogue discontinued. The situation balances on the verge of a massive Russia-NATO conflict. Finland and Sweden join the alliance and offer unconditional military support. The scenario is also likely if one of the sides loses the local conflict.

**Scenario 4.** The security dilemma shrinks. The set of common or specific challenges make mutual containment hurtful for both sides that switch to confidence-building measures. The Donbas conflict remains but acquires a positive dynamic. Russia and the United States selectively cooperate in the Middle East. Mistrust still exists, with the uncertainty level gradually goes down.

**Scenario 5.** An overhaul of relations is initiated by a side to improve the situation. Such steps are likely to be related to the role of a concrete political leader or leaders, which are to overcome the resistance of the containment-oriented institutions. We see a drastic revision of Russia's relations with NATO and the EU, as well as a compromise on the Donbas settlement. The sides launch a review of the Founding Act, work to strengthen the OSCE as the Europe-wide security institution, and discuss conventional armaments control. NATO is reformatted to counter new challenges.

Scenarios 4 and 5 are highly unlikely. Scenarios 2 and 3 seem suitable for the current state of affairs but are also unlikely because of the high price for both sides. Most probable seems Scenario 1 which allows for some low-cost muscle flexing. ■



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# Highlights of the current state of international relations in Baltic Sea Region

Expert article • 2151

A feature of the current global trends is their high degree of unpredictability. The Baltic Sea region is no exception, though it has stayed relatively calm for quite a while.

The EU has faced considerable challenges, which may require some major internal reforms. It is possible that the changes would affect not only the institutions and their interaction with the member states, but the very makeup of the EU. Though having a separate stance on certain issues, the countries of the Baltic Sea region in general will support efforts toward strengthening the EU. It seems that the EU transformation will succeed; yet, it might be accompanied by slowdown, if not a temporary backtracking of European integration. The EU will focus more on the internal issues, laying aside the external ones, e.g. its relations with Russia. Clearly, the EU policy to apply the same standards to Russia as to candidate countries, making special emphasis on civil society rather than strengthening interstate relations, has proven unsuccessful. Yet, the EU is unlikely to come up with a common strategy on Russia. Hence, in the short term, no initiatives capable of changing the status quo in the Baltic Sea region are likely to come about. Most probably, the EU members will reach consensus on just a few concrete steps regarding Russia.

In the United States a priority reassessment is underway too. The Donald Trump Administration is absolutely sure to revise U.S. policy in Europe from the perspective of making it more efficient. The TTIP negotiations will end, or at least be put off indefinitely. The dissolution of NATO is unlikely; however, Trump will try to reorientate the Alliance to combatting terrorism as priority and demand that the allies increase their military spending. The Baltic Sea region NATO member states are likely to go with it. Of more complicated nature is the issue of whether or not the Warsaw Summit decision to deploy the four battalions to Poland, Lithuania, Latvia, and Estonia will stand. In any case the United States is sure to continue developing bilateral relations with the Baltic Sea region countries, including Finland and Sweden. Finally, Trump is likely to reactivate the deployment of the ABM systems, particularly in Poland. At the same time the Baltic Sea region is unlikely to become a priority for the United States beyond the wider context of U.S. relations with Russia.

With a major role in the Baltic Sea region, while being neither a member of NATO, nor the EU, Russia finds itself in a serious confrontation with both of them. Though socio-economic situation in Russia may be difficult in the coming years, its political stability is likely to persist. However the gap between the standards of living in Russia and in other countries of the Baltic Sea region will continue to widen. The military factor plays important role in Russian policy in Baltic Sea Region. The military exercises staged in Russia's North-West and the repositioning of troops and military equipment to Kaliningrad to a great extent reflected the apprehension by the Russian ruling circles

about the elements of the American ABM systems being deployed in Poland, as well as their desire to reassert Russia's possession of the Kaliningrad region and to strengthen Russia's diplomatic potential before any future talks. Of particular significance is Russia's vested interest that Nord Stream should remain in operation – gas export revenues add significantly to Russia's state budget. Overall, Russia is unlikely to resort to radical measures capable of changing the situation in the Baltic Sea region.

Further deterioration of relations in the Baltic Sea region is unlikely – it simply does not follow from the logic of the latest events. Destabilization by external factors (e.g. the Syrian and Ukrainian conflicts, the immigration crisis, and etc.) cannot be totally discounted, but the probability is not very high. Still, there is little potential for improvement. The air of mutual suspicion and the lack of trust between Russia and the other Baltic Sea region countries could get in the way. Alas, one cannot exclude the possibility of a military incident taking place as a result of a contingency or a technical failure. Yet, a chance that it would lead to a full-blown war is tiny. Much will depend on the relations within the triangle Russia-EU-USA. In our view, the current period of poor relations between Russia and the EU is anomaly with the general development of relations throughout Europe – a process spanning centuries and driving by not only on political, economic, and humanitarian relations, but by common civilization roots. Yet, normalization of relations will not be easy. Some improvement is possible, but cardinal changes can come only over a medium term. ■



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# Securing Nordic Arctic sustainable development – Arctic cooperation in the Nordic realm

Expert article • 2152

**N**ordic Council of minister's Arctic priority dates back to 1996 when the parliamentary Arctic cooperation committee continued its cooperation with Canada, Russia, USA and the European parliament in the wake of the establishment of the Arctic Council that has just celebrated its 20th anniversary. From the early start of this cooperation the main focus was cross-border concerns and questions related to sustainable development in the Arctic where environmental pollution and development of Arctic cooperation networks, as well as the concern for Security policies were prominent. The two first mentioned priorities have been a red thread in the efforts of the Nordic Council of ministers (NCM) ever since, even if there have from time to time been variations in what is considered a main priority or so-called "horizontal policy" of the Council affecting Arctic Cooperation.

The Nordic Arctic Cooperation programme (NACP) was initiated and from then on became specially prioritized in the Councils funding efforts, along with culture (which is most prominent support area) education, research, environment and the neighbouring areas (i.e. Baltic states). The programme has since 1996 resulted in many hundred projects, Arctic activities and political initiatives that range from climate change, environment and nature, economic development, sustainable development of health, culture and competences. The Arctic council permanent working groups and affiliated secretariats have benefitted from the programme in their work. The programme has since 2012 contributed with approximately 5 million DKK to the work of Arctic Council's working groups, task forces, expert groups and support to permanent participants' projects.

The current program period 2015-2017 is ending this year. Its aim is securing sustainable development with respect for nature and welfare for humans living in the Arctic. Applicants for funding have applied for projects within one of four prioritized themes that encompass subjects within the themes of population, sustainable economic development, climate, environment and nature, and education and skill enhancement. The next program period starting 2018 is now being drafted and the previous program period is being evaluated and revised.

## Nordregio's Nordic Arctic Working Group

In 2013 the regional sector of the NCM wished to initiate a thematically broad and in-depth study of the future development of the Arctic using possible scenarios. The objective of this work was to provide input to the further development of the NCM Arctic Cooperation Programme by collecting, reviewing and analysing existing information, assessing different preconditions for future development in the area and developing future scenarios. This work that has now been ongoing since and was completed ultimo December 2016 will feed into the political debate and give more holistic overview of the scientific knowledge.

From the beginning this project took the bottom up approach and involved local and regional stakeholders, as it is our believe that Arctic future perspectives should be developed by the population of the North. We applied a foresight method organising workshops in 12 case study regions around the Nordic Arctic; Greenland, Iceland, Faroe Islands, Norway, Sweden and Finland. We then brought the summarised results to a forum of regional and national stakeholders and representatives who also contributed with their vision next 10, 20 and 30

From the beginning this project took the bottom up approach and involved local and regional stakeholders, as it is our believe that Arctic future perspectives should be developed by the population of the North.

years ahead for the involved regions. At last we mobilized a dialogue in the West Nordic Council and with the North Calotte Council on what aims and strategies should be developed to secure sustainable regional development. As background material we have collected data and produced comparative maps on i.e. demographic development, economic development, occupational development, skills development and entrepreneurship. Comparison that hopefully proves useful to politicians and planners in the Nordic region, in dealing with the opportunities and challenges ahead in a rapidly changing region.

We identify a number of interesting opportunities that are contributing to a fundamental change of economic dynamics within the Nordic part of the Arctic. Current challenges for the Nordic Arctic include a lack of diversity in economic activities, investments and human resources. However, young people in the Nordic Arctic are adapting to new multi-locational lifestyles, dividing their time between home, work and studies in different locations. This is becoming the new normal among Arctic youth, especially those who are not willing to leave their

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homes in remote areas to move permanently to bigger cities. The potential for knowledge intensive job creation is limited as the lack of broadband connection hinders distance learning. More young women than men pursue higher education; thus, more women than men leave the Nordic Arctic.

What our three year study reveals, is that Arctic areas hold several economic opportunities for young people in less traditional industries like the creative industries, bio-economy and tourism.

Primary industries have traditionally been the foundation of the Nordic Arctic economy, but our study shows that huge potential lies in less traditional industries. Sustainable natural resource extraction forms the basis for more recent business opportunities, like the bio-economy and more knowledge-intensive activities such as research, development and innovation. Growing industries like responsible tourism and creative industries, also show promise – for example cultural events, locally produced food, handicrafts, art and film production.

Access to vocational and higher education opportunities, as well as lifelong learning, is fundamental for individual development and for the competitiveness of companies in the Arctic regions.

The Nordic Arctic region has the potential to become internationally established as a forerunner for sustainable business development, innovation and research. The focus is increasingly on upgrading bio-resources to produce, for example, feed and food ingredients, biomaterials and biofuel. Bio-refining contributes to the renewal of

existing forestry industries and is seen as a mechanism to support regional development. The marine sector naturally plays a crucial role in the bio-economies of Iceland, Greenland, the Faroe Islands and the coastal regions of Norway and there is potential to develop an innovative marine industry, based on algae and bioprospecting and creating side-products from primary production.

I believe that Nordic cooperation on Arctic development is likely to remain strong with the revised Nordic Arctic Cooperation programme as one of the Councils tools to support sustainable regional development in the Arctic. ■

More extensive reading can be retrieved at: <http://www.nordregio.se/en/News/Launch-30-January-Arctic-Future-Perspectives/>



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# Continued collaboration and vigilance against tuberculosis in Russia

Expert article • 2153

**T**uberculosis, an infectious bacterial disease primarily affecting the lungs, is the second-highest cause of infectious disease death in the world (after HIV/AIDS). Russia is one of thirty countries currently designated as “high TB-burden” by the World Health Organization. In 2015, there were about 115,000 new reported cases of tuberculosis in Russia. Overall TB incidence and mortality rates have stabilized and even declined in Russia over the last decade, thanks largely to smart government policy and the introduction of modern treatment methods spearheaded by international partners. Continued vigilance and support is essential, however, due to the evolving nature of the Russian and global TB epidemic.

The crisis around TB in Russia originated with the disintegration of the Soviet Union and the country’s consequent social deterioration. Government TB control programs faltered. The number of both new cases and deaths attributable to TB skyrocketed throughout the 1990s. Overcrowding and poor ventilation in the country’s penitentiary system turned it into an exemplary breeding ground for the disease; over a quarter of new cases in the late 1990s were among prisoners.

Russia’s economic recovery and therefore availability of new domestic resources, in addition to funding from the World Bank and Global Fund and technical assistance from the World Health Organization and numerous non-governmental organizations, turned things around beginning in the early 2000s. Treatment methods based on directly observed chemotherapy, modern diagnostic standards, improved case registration, and reliable drug supplies were introduced. Russian government financial commitment to TB control has been impressive: over a billion US dollars annually from federal plus regional budgets in recent years, representing well over half of all TB expenditures in the WHO European Region.

Yet Russia remains one of the world’s most worrisome incubators of multi-drug-resistant TB – a form of the disease that is untouchable by the most common, inexpensive antibiotics. In 2013 (the most recent year for which reliable data are available), almost one-quarter of new Russian TB cases, and over half of previously treated cases, were drug-resistant. Only a handful of other countries, all of them Russia’s neighbors, have comparably high MDR-TB burdens among new TB cases (Ukraine, Belarus, Kazakhstan, Kyrgyzstan, Uzbekistan). Extensively-drug resistant TB (XDR-TB), which is even more difficult and expensive to treat, is also growing, now representing about 2% of new Russian TB cases. And the increasing number of Russians afflicted with both TB and HIV is presenting a new challenge to health and social service systems: about 10% of Russian patients newly diagnosed with TB were also HIV-positive in 2015. Services for people who use injection drugs – a major risk group for both TB and HIV – remain wholly inadequate, highlighting inequities in access to diagnosis, treatment, and care for vulnerable groups of all kinds. Indeed, the HIV-TB-drug use syndemic represents both a medical and a human rights challenge in the Russian context.

For Russia’s neighbors, this is not just a humanitarian concern. According to the European Centre for Disease Prevention and Control in Stockholm, one-fifth of the notified cases of MDR-TB in European Union countries in 2010 were among individuals of foreign origin. Of the TB cases of foreign origin diagnosed that year in the ten EU countries located at the EU’s Eastern border, fully half were from Russia; although the absolute numbers remain relatively small, the ECDC study cautions that increasing migration from the East may push these totals higher. Research based at Helsinki’s National Institute for Health and Welfare has demonstrated an increase in the proportion of immigrant cases of (non-MDR) TB identified in Finland, from around 6% in 1995 to one-third in 2013, with Russia the second most common source country (after Somalia).

In an increasingly complex political environment, the imperative for cooperation on an issue of such straightforward mutual interest is strong. Moscow’s hosting of a WHO ministerial-level meeting on TB in November 2017 should provide a spotlight and catalyst for action. Evidence-based, cost-effective treatment and prevention, based on structural improvements to facilities, more rigorous laboratory and clinical protocols, and social support for already-vulnerable patients, has prevented and/or reversed MDR-TB epidemics in Latvia, Estonia, and even some individual Russian provinces. Scientific research collaboration between Russian and European partners on TB is robust but could benefit from even more support. The same is true for policy dialogue, particularly around screening, prevention, and intervention protocols governing migrants, drug users, and other at-risk populations. Infectious disease knows no borders; neither should action to prevent and reverse its spread. ■



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# Geopolitical repercussions of a changing world order on Russian-EU relations

Expert article • 2154

Looking closer at the present state of both the European Union and the Russian Federation we can make out that they are equally product and subject of **two unfinished transformational processes** which are shaping the destiny of Europe amidst fundamental changes in world politics. The collapse of the USSR and the signing of the Maastricht treaty in 1992 set off two interconnected transformations which run through adverse stages and are far from over yet. And in a twist of history, two geopolitical actors were formed, the EU and Russia which differ fundamentally in their socio-political, and normative nature. Such differences are a major reason for misunderstandings leading to antagonistic narratives and conflicts.

## Russia's unfinished and contradictory transition

Post-Soviet Russia survived barely the dreadful 1990s, exposed to a permanent systemic crisis, and almost considered a failing state. Only owing to externally induced economic growth and partnership with the EU, Moscow was able to restore state authority, achieve political stability and societal consolidation. Historically, to use Robert Coopers' terminology, for the first time a *modern Russian state* was created.

Undoubtedly, whether we like it or not, today Russia is back in from the Cold and to the surprise of Western powers moved within a short period of time to a key position as a powerful actor with sovereign national interests. Moscow's reappearance altered international power constellations and reinforced transformational trends, weakening the unipolar world order. In this regard, Russia is a *revisionist power* following a path of *multivector policies* which are triangular shaped: the core idea is to maintain good relations with Washington, the EU and China. However, within its triangular shape, the focus may shift according to the rise of opportunities or the worsening of relations. The contradiction between Russia's performance in international politics and her accomplishments in domestic matters, especially the low level of economic progress, is striking. In economic terms the country is a dwarf. 25 years after the end of the USSR, Russia is still an energy and raw material appendix of the developed industrial OECD-world.

On that account, Russia can only be described as a superpower in military terms. The Kremlians relapse into imperial ambitions, as often assumed in Western media and politics is neither realistic nor attainable. As a modern state pursuing national interests, Moscow bases its foreign policy objectives on hard power instruments and acts accordingly. Even Brzezinski agrees: "Russia is no longer an imperial power, and its central challenge is to recover socioeconomically..."<sup>2</sup>

<sup>1</sup> Robert Cooper, *The Breaking of Nations, Order and Chaos in the Twenty-First Century*, London, 2003, P.16.

<sup>2</sup> Zbigniew Brzezinski, *The Choice: Global Domination or Global Leadership*, New York 2004, P.3.

For that reason, as long as Russia does not overcome her technological and industrial backwardness, and comes to terms with forming peaceful, cooperative links or promotes mutual security relationships with her European partners, the country will not be invited as an active partner in shaping a European peace order.

## A reluctant geopolitical player: the European Union and her twisted relationship with Russia

In comparison to Russia the European Union took a different course of development. Over a period of more than three decades, and passing through various stages of transformation European integration produced a *post-modern* socio-political entity<sup>3</sup>, the European Union. Economic success, social cohesion and political stability created a zone of peace which allowed an alternate approach to external affairs not based on hard but on soft power to achieve objectives.

But today the EU ended up in an appalling state of internal disunity, rising protests and split societies, which immobilize external activities. Political will for restructuring is missing. But if restructuring fails, the EU will be more an object of multipolar tendencies than a driver for shaping the global project. Eventually the EU may be forced to sway in between different poles.

To avoid such a depressing scenario to happen, improvement of Russian-EU relations is crucial. Of top political priority is the solution of the Ukrainian crisis through a negotiated and commonly approved settlement. Regardless how difficult it may be to implement all the 13 agreed points at once or subsequently, there is no alternative to the Minsk II agreement. But we need as well to reflect the causes for the deterioration of the EU-Russia relationship?

Among others two aspects played a key role wrecking the previously reasonably relationship between the two geopolitical European actors:

1. From 1992 until 2009 the EU's Eastern policy was based on core principles of Germany's Eastern policy which served as a surrogate for Brussels' lack of strategic orientation what to do with Russia. Pragmatic partnership and cooperation on all levels of economic, social, political and cultural life was the core idea.
2. Given its deplorable socio-economic backwardness Moscow followed the lead of Brussels. Simply by close collaboration with EU-member states Russia could achieve goals of modernization. "Partnership in modernization" was the catchword, which suited both interests. Sergei Karaganov defined the ultimate objective of Russia's external path: "Close interaction with the EU remains an imperative of Russia's policy"<sup>4</sup>.

<sup>3</sup> Robert Cooper, *The Breaking of Nations, Order and Chaos in the Twenty-First Century*, London, 2003, P.16

<sup>4</sup> Sergei Karaganov, *New Contours of the World Order*, in: [Russia in Global Affairs](#), Nr 4, October - December 2005

However, history took the liberty to veer of its course. The pragmatic, cooperative and interests based EU policy changed roughly about 2008 *toward a confrontational track focussed on normative goals*. The following factors may explain the change:

- Central European countries attempted to redesign the EU's Russia first policy. The question who should dominate the EU's Eastern policy moved on to the agenda.
- Germany underwent domestic political changes: the Social Democrats were replaced as a coalition partner and succeeding the political basis of Ostpolitik was undermined.

These developments led to a colder and confrontational relation between Russia and the EU. The Russian answer followed promptly: A shift of paradigm occurred as well in Russian foreign policy and slowly gained momentum. The Kremlin simply lost hope once being accepted as an equal partner by Western powers, and sought alternatives in Asia and with other emerging nations.

### How to shift course toward a pragmatic, trust based relationship again?

Lessons from the Ukrainian crisis can be drawn. Above all the conflict lay bare that the creation of antagonistic block structures (EU versus EEU) will lead to mutual aggressive policies and foster destructive nationalist sentiments. On the base of "antagonistic" relations with Moscow, neither the territorial integrity nor political security or economic rehabilitation of Ukraine can be secured. To escape from such stalemate, a robust European security architecture including Russia must be constructed. Territorial integrity and protection of the Ukraine must be secured and guaranteed by all participating actors and based on strong economic interdependence of EU and EEU. To achieve such guarantee would be the litmus test for embarking on a Road Map toward comprehensive European security.

Above all, the Ukrainian conflict demonstrates the need to build a *clearing house in Russia-EU –relations* better equipped but analogous to the NATO-Russia Council. Conflict prevention, shared information and cooperation to counter radical and fundamentalist threats to European security should top the agenda.

Further, it seems to be clear that no conflict in CIS is solvable without Moscow's participation. What's even more pressing for the EU, the Minsk II agreement would collapse the moment Moscow would withdraw its support. ■



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# Coherence between the interests of Russia and Germany in the Baltic States

Expert article • 2155

The economic relations between Russia and the Baltic states today are at a more advanced level than the political dialogue. That state of affairs does not contribute to promoting the regional interests of Russia. Geo-economic analysis shows that exploitation of the Baltic vector of German economic policy can become the most significant factor of promoting Russian interests in the Baltic.

On the basis of Baltic Federal Immanuel Kant University, supported by the Russian Foundation for Basic Research, today we implement a research project aimed at correlating the foreign-policy doctrine of Germany in relation to the Baltic States at the current stage and possibilities for promoting political, economic, social and human interests of Russia in this region. During the process of research, we have encountered some methodological difficulties. The most basic ones, in our point of view, may include the problem of dynamics and instability of interests; divergent discursive fields of Russia, Germany and the Baltic states towards the region; restrictions in the use of the measurement tools of comparative studies in the sphere of international affairs.

The coherence of positions of Germany and the Baltic states towards Russia is quite low and relates mainly to the political aspects of multilateral relations in the region. Non-political spheres may be regarded as the case of even lower coherence of the interests of Germany and the Baltic states. Russian initiatives to develop tolerance and resist to radicalism are well regarded by the range of European partners. The governments of the Baltic States see such initiatives as an intervention in their internal affairs. Effective influence on changing the situation of Russian-speaking community in the Baltic States is possible in conditions of understanding the problem of two main regional states – Russia and Germany – more closely. The closest to Russian understanding of the idea of tolerance is such a specific priority of German Baltic vector foreign policy, as strengthening of regional identity. Baltic identity is interpreted from an axiological point – as a sense of belonging and building shared values, and institutionally – as following common rules and standards of relations. From the perspective of Berlin, “Baltic community” (Ostseeschaft) can and should include ethno-linguistic diversity, which coincides with position of Russia, but is contrary to it at the same time, because severely faces the policy of inviolability of Russian identity in Kaliningrad region. The problems of outward investment, maintaining the level of trade between countries, establishment of pan-European and regional autonomous energy system, the issues of supplying Russian energy and electricity showed themselves as the common ground of regional interests.

The interests of Russia and Germany are most coherent in the Southeast Baltic States. The common priority of the countries are stability and regional development. The instruments of German partnership policy are structuring the fund of project finance, pilot financial initiative, collaboration in the context of civil society, facilitation of contacts between people and Visa Regime simplification, and investment promotion. One of the directions of German activity in Kaliningrad region is tourism, particularly the development of the cruise tourism.

The content analysis of bilateral and multilateral relationships between Germany, Russia and the Baltic states allowed us to reveal the considerable implementation gap in regional projects of collaboration from direct bilateral agreements. The promotion of Russian regional interests in the Eastern Baltic States is accompanied by visible asymmetry of economic and political positions in relationships with Germany and the Baltic states. This state of affairs provides the opportunity of exploitation the Baltic vector of German foreign policy for our country. The most promising appears the so-called “strategy of tiny actions”, the essence of which can be reduced, in general terms, to depoliticization of the Russian-German economic cooperation in Baltic region and to economism of socio-cultural connections undermining the institutions of the Baltic states’ civil society. The sphere of collaboration on the level of particular regions of countries and municipalities remains opened, despite the complication of political relationship. The potential of such a collaboration, in our point of view, is underestimated. Projects in the sphere of culture (the ones that support cultural diversity), science (medicine and agriculture), business-education and ecology may become the fields of regional cooperation. ■



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# Where are Russia's national minorities?

Expert article • 2156

The growth of Russian assertiveness based on a vision of the Russian nation linked to Russia's historic role as a great power is evident for all to see: an assertive patriotism, the leading role of the Russian Orthodox Church, and a foreign policy informed by a sense of responsibility to ethnic Russians living abroad, have raised their intensity since the Ukraine crisis developed towards the end of 2013.

Against this background, Russia's national minorities, with the exception of the Kadyrov-led Chechens, have been strangely silent. Strange, because non-Russians make up almost 20% of Russia's population according to the 2010 census; because it is possible to count close to 200 national minorities; because many of the larger ones retain the institutional buttress of the status of a national federal unit inherited from the Soviet Union; and because it is difficult to see what they have to gain from recent developments. At least some opposition to current developments, which seem to heavily favour ethnic Russians at least in the rhetoric and climate of the day, might be expected.

Today's situation is, to some extent, a reversal of what it was twenty to thirty years ago. Then, minorities were vocal and proud, and gaining unprecedented levels of self-rule, while the idea of the Russian nation was lost in bewilderment at the collapse of the Soviet Empire. In the last years of the Soviet Union, smouldering resentment among the population of the Baltic republics against the Soviet occupation of their land burst into the open. This inspired other minorities to nail their economic and environmental grievances to the national mast.

As the Soviet Union ruptured along the lines of its major nationalities, smaller groups put forward their own claims. They were encouraged to do so by Boris Yeltsin, who called on minorities to 'swallow as much autonomy as you. Whether Yeltsin's declaration was sincere or opportunist as long as he was leading opposition to Gorbachev, as President of post-Soviet Russia circumstances ensured that he stood by its implications. Faced with Chechnya's attempt to establish independence, Yeltsin sought to prevent similar moves elsewhere by enshrining the status of national republics and regions in the new Russian constitution of 1993, while negotiating high levels of self-rule with individual national territories, most notably the largest of them in terms of population, Tatarstan.

National minorities celebrated their rights and freedoms, their existence and cultures were put on open display, and their representatives made ties internationally. The Russian state under Yeltsin, meanwhile, appeared to be moving towards embracing a broad and inclusive civic (i.e. non-ethnic) version of Russian identity.

On a simple reading, these processes were gradually but systematically reversed by Yeltsin's successor. One of Vladimir

Putin's first moves as President of Russia was to create seven new 'super-regions' for Russia which ignored the national element. This was followed by reform of the Federal Council that gave less of a voice to the regions, and measures to give the President greater control over the appointment of regional governors and assemblies. Meanwhile, the Constitutional Court busied itself in reversing the principle of national regional sovereignty. Federal reform led to the disappearance of some of the smaller national autonomous units, and the teaching of minority languages declined rapidly.

Political parties based on ethnicity have also been banned since 2001. Taken together, these measures eroded the institutional base and power of national minorities and their ability to flourish culturally and express themselves politically. Acts of individual and mass violence against non-Russians, although often directed against migrant workers from Central Asia, have also contributed to an intimidating atmosphere.

As always in Russia, however, there are contradictions all across this picture. Russian nationalism was strong enough in the early 1990s to give significant electoral success to the nationalist Vladimir Zhirinovskiy, while racism against Muslims from the Caucasus was evident in Moscow and elsewhere well before the Chechen conflict erupted into open warfare. On the other hand, Putin has consistently stressed that Russia is a multi-national state, and national territories and education persist. Minority cultures are still supported by state funding and remain visible and celebrated across Russia.

The current passivity of non-Russian minorities can in part be explained by this contradictory situation: the 'folklorisation' of minorities, as describe in a report to the Parliamentary Assembly of the Council of Europe in 2006, is a method of providing an outlet to minority identities. As Glasgow University's Federica Pina has argued, this effectively divorces minority questions from politics. Several national activists object to the activities of state-sanctioned cultural organisations such as the organisation 'Regional Tatar National-Cultural Autonomy'. But such voices remain marginal at present. Whether a further surge in nationalism might goad Russia's national minorities into a more vocal reaction remains to be seen. ■



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# Heritage in flux: Europeanization as identity politics

Expert article • 2157

In the context of the European Union's (EU's) Eastern enlargement, European identity politics has become very topical. During the enlargement process the candidate countries were conceived to graduate to 'Europe proper' after proving their will and capability to internalize European values and norms. However, further developments have shown that in practice the process is never a linear one, since the new member states also mold the EU. Current ongoing debates about the meanings of 'Europe' and 'European' in the different EU countries can be seen as one example of that.

In parallel with the enlargement process, European integration developed from the economic and political sphere to the cultural one, a development framed as cultural Europeanization. Culture was made an official policy sector of the EU in the Treaty of Maastricht. Since then various initiatives have been launched that legitimize and justify cultural integration of the EU as part of European identity politics. Forming and enshrining a European cultural heritage has been one cornerstone of this process.

The most recent example of fostering a cultural heritage as part of EU identity politics is the European Heritage Label (EHL) initiative launched as an official action by the European Commission in 2011. The labeled sites are pre-selected at the national level and the final selection is made by an expert panel appointed at the EU level. To date, the label has been designated to 29 sites. Since twelve of the designated sites are situated in countries that have joined the EU during the last Eastern enlargements—Croatia, Czech Republic, Estonia (2), Hungary (2), Lithuania, Poland (4), and Slovenia—the EHL also brings together different forms of Europeanization.

The heritage sites spring from different epochs of time; from the Neanderthal period, through the medieval time and World Wars, to the fall of the Iron Curtain. From the recent period preceding the EU's Eastern enlargements, the Gdansk Shipyard in Poland, where the Solidarity (*Solidarność*) movement was established, is designated. Similarly, the memorial park on the Austria-Hungary border, where a peace demonstration was held in 1989, is praised for its significance to a borderless and unified Europe.

Apart from the temporal difference, the sites also represent different institutions. Museums are widely represented among the sites. For example, the Great Guild Hall, situated in Tallinn, Estonia, represents Hanseatic architecture and currently hosts the Estonian History Museum. Also the Franja Partisan Hospital from World War II has been turned into a museum. The Olomouc Premyslid Castle and Archdiocesan Museum in the Czech Republic focus on the Moravian presence in European history.

On the other hand, the historic ensemble of the University of Tartu in Estonia functions as a university campus. Similarly, the Ferenz Liszt Academy in Budapest, Hungary is an international university of musical arts and also a concert center. The Lithuanian site, Kaunas of 1919–1940, praises the prosperous development of the city into a modern cultural center during the time period when it was the temporary capital of the country.

Unlike the UNESCO World Heritage List, the main objectives of the EHL are to bring to life a European narrative and promote the European dimension of the sites. However, all the sites also stand for a remarkable national heritage. The same holds true in the level of actors. In practice, the European cultural heritage is formed in an interplay between the EU and national levels: since the daily practice of the sites is managed by national actors, they also have a significant role in mapping the meanings of Europe. This can be done by framing what the European dimension of the sites means and how the European narrative is told.

Furthermore, the process is a good example of how Europeanization and promotion of the national dimension become entangled in identity politics by different actors. For example, in the site videos available on the European Commission website, apart from the European aspects of the sites, national ones are emphasized. As part of the process, the meanings of Europe as well as the relationship between national and European are continuously in flux. Therefore, in identity politics, like Europeanization, nothing can be taken for granted: instead of identity as a status quo entity, multilayered and often controversial processes at the European and national levels deserve the main focus. ■



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# Company towns in Russian Federation

Expert article • 2158

**D**uring the 2007-2009 financial crisis, Russian company towns (or “monotowns” – the so called single-industry communities) became the potential source of social tension and oppression. Some of the company towns, which basically were build around certain enterprises to provide the employment needed, became useless due to variety of reasons: poor performance of the enterprises, lack of competition and poor infrastructural conditions. Whereas the fear of the consequences of the company towns’ crisis was exaggerated for the rest of the world, for Russia, the problem still has its reasons for the further concern.

Since the end of 2014, the Russian Government compiles a list of the most vulnerable company towns. By the beginning of 2016, the list was comprised of 319 company towns (out of almost 1100 towns across the country). There are three key categories in this list, depending on the level of socio-economic vulnerability: the most vulnerable company towns (1st category), company towns with the risk of deterioration (2nd category), and last category consists of company towns with stable economies. In the mean time, there are certain swings back and forth in the company towns between those categories, which means, that all of the company towns do have some issues in common.

One of the main reasons of company towns’ vulnerability is the production of noncompetitive goods, along with the extremely high costs of production. This gives rise to a more serious problem — the insufficient amount of qualified human resources — which hampers the acceleration of company towns’ revitalization (in the cases when there are grounds for revitalization). Plus, some of the company towns suffer from the internal migration, for instance, in the Far East Region, there were numbers of company towns that had to be reclassified to the villages, since there was a massive drain of the workforce to the more urban communities.

In the meantime, the company towns’ development is vulnerable to the slightest fluctuations in the environment and has no ability to resist negative external effects. Changes in the external market situation, decreasing demand, as well as plummeting prices of goods sold by the town-forming company can cast a company towns’ economy in a state of acute crisis, which may only be overcome by using significant financial resources. The statement is proven by both the economic instability of the 1990s and the 2008—2009 economic and financial crisis: the socioeconomic situation in company towns was the most depressive throughout the country; at the same time, company towns affect the economic situation nationwide. According to some estimates, the actual unemployment rate in Russia ranged from 7 to 7.5 % at the beginning of the 2008 crisis, whereas in company towns it reached approximately 30 %.

It is worth noting that there are some ways the Government is trying to cope with the company towns. For instance, there are three

major types of initiatives: the first one is based on the financial backing for the town-forming enterprises, which are crucial for the national economy and national security. Another way is related to the federal agencies’ initiatives: specific labor programs for the company towns’ citizens (from the Ministry of Labor and Social Protection), subsidies for the industrial enterprises (the Ministry of Industry and Trade), etc. Finally, due to the Russian Government Decree (No. 473 FZ<sup>1</sup>), some of the company towns are worth being named as “advanced development territories” – if one town gets this “status”, it also gets certain taxation privileges, special legal regimes for business and other activities (rent exemptions, tax privileges, and special regimes of public and municipal control) and withdrawal of land for advanced territories’ buildings and infrastructure. It is not the time to make any considerations on the usefulness of such initiatives: we shall see in the nearest future whether the new approaches of the Government for creating the system policy towards company towns is successful or not.

Yet, it is not quite clear, what are the compliance criteria for the “advanced development territories” status? For this reason, there is at least one set of issues we might want to think about: the problem of opportunism and the information asymmetry problem. For example, what if those privileges create wrong incentives, and regions which do need the “advanced” status do not get them, because some regions hide certain information on their actual performance, hence, they get the status? Therefore, it is important to understand the possible mechanisms of deterring the opportunistic behavior in such cases, and, maybe, it is time to look for the completely new concepts that may help devising the system policy towards the Russian company towns. ■

<sup>1</sup> FZ – Federal Law (Federalny zakon – rus.)



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# China's One Belt One Road (OBOR) initiative: a win-win situation for the Baltic Sea Region (BSR)?

Expert article • 2159

Since the launch in 2013 of China's two-pronged OBOR initiative which aims to reshape and boost trade links between China and Europe through enhanced physical and digital connectivity along the land-based *Silk Road Economic Belt* and the ocean-going *21st Century Maritime Silk Road*, BSR countries have embraced the initiative with increasing enthusiasm to make the most of new economic and geopolitical realities.

In 2016, Latvia for example hosted the first meeting of the transport ministers of 16 Central and Eastern European countries (CEECs) and China, dubbed the '16+1 cooperation format', established a CEEC-China secretariat on logistics cooperation in Riga and hosted the 5th Summit of the Heads of Government of the 16 CEECs and China. The Summit inter alia launched the Adriatic-Baltic-Black Sea Seaport Cooperation which seeks not only to intensify north-south cooperation in the development of sea ports, including industrial parks, transport corridors and infrastructure connecting the CEECs with China but also to contribute to synergies between China's OBOR, development strategies of CEECs and the EU Trans-European Transport Network (TEN-T) projects. As side-events to the Summit, a Business Summit and a symposium of think tanks were organised in Riga. The symposium provided an opportunity for academia to take stock of the achievements and shortcomings of China-CEEC cooperation which could feed into the future relationship between BSR countries and China.

Latvia has thus been one of the most proactive BSR countries in bringing to bear its comparative economic advantages as well as its geostrategic position as a logistics and transit hub for China's trade with the Nordic countries. A genuine 'win-win situation', however, is still far from being achieved. Chinese exports to Latvia increased by

an impressive 17.7% to €415.1 million in 2015; this contrasts sharply with the far more modest growth in Latvia's exports to China which grew by a paltry 0.4% to €105.9 million over the same period according to Latvian data.

## The BSR linking up to the China-Europe freight train lines: prospects and challenges

Since 2011, when the first YuXinOu Railway cargo trains started to run between Chongqing (Sichuan province in the southwest of China) and Duisburg, Germany, new freight train lines directly connecting different Chinese and European cities have mushroomed. In November

2016 the first pilot Chinese Railway Express train from Yiwu (Zhejiang province on China's east coast) arrived in Riga, thereby extending the China-Europe freight rail lines further into the BSR where they meet with the EU-co-financed high-speed rail project Rail Baltica.

The revival of the railway system has created new opportunities for rail freight transport providers in a market niche of high value-added products which can be more efficiently integrated into the international logistic supply chain. A 2011 OECD report on trans-continental infrastructure

needs to 2030/2050 estimated that a maximum freight container volume ranging from 0.5 to 1 million TEUs (Twenty-Foot Equivalent Unit) per year could be transported along the route from Asia to Europe. This is small compared with the current maritime volumes of about 20 million TEUs shipped on Asia to Europe sea routes per year. Shorter delivery time compared to maritime transport, lower transport costs and CO2 emissions compared to air transport have convinced some manufacturing companies in various high value-added sectors such as Hewlett-Packard, Intel and Acer to shift to rail transport services.

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The rail transport development has been driven by China's domestic development policies of transferring labour-intensive production facilities from its prosperous coastal provinces to less industrialized western and central provinces both to narrow socio-economic discrepancies within the country, but also to benefit from lower labour costs in order to retain China's competitive edge over its low-cost Asian peers such as Bangladesh, Cambodia, Thailand, and Vietnam. It is also part of China's ambition to reduce its dependence on maritime transport that accounts for the vast majority of its trade and energy imports given China's fears of maritime transport disruptions at US-controlled chokepoints like the Strait of Malacca, if there were a conflict with Japan or the United States.

China's aim is also to explore new sources of growth for its slowing economy by tapping into new export markets for Chinese consumer goods but also for infrastructure construction companies which sit on huge overcapacities of steel, cement, aluminium, glass, paper, and other building materials. The Chinese government strongly backs cargo rail transport under the OBOR initiative – including by heavily subsidizing rail freight tariffs – and has successfully pursued policy coordination with the members of the Eurasian Economic Union which has resulted in a common rail cargo tariff. This has sparked competitive dynamics in Chinese provinces which are eager to exploit business opportunities along new cargo rail lines through Central Asia to Europe. The critical mass of westbound rail cargo in turn has encouraged European partners to seek further efficiencies in terms of transport time and cost through technological innovations.

However, so far the bulk of rail containers which arrive with a full load from China (mostly capital-intensive goods such as automotive parts and electronics) return empty or pile up at European terminals for lack of demand for eastbound rail transport. This may reflect the unsuitability of eastbound goods for rail transport and the asymmetry characterising the trade relations of most countries with China. According to Kazakhstan Railways, westbound trains transported 32.179 TEU, while eastbound trains carried 17.744 TEU in 2015. Hence, better capacity utilisation for eastbound rail freight seems to require further action, including trade promotion activities in China to boost BSR exports. Here again Latvia has taken the lead by establishing an office of its Investment and Development Agency in China's port city Ningbo (Zhejiang province) in 2016.

Conferences jointly organised by associations such as the East West Transport Corridor Association (EWTC) and the China International Forwarders Association (CIFA) in September 2016 in Vilnius and Klaipeda under the title 'Silk Road Connecting China with Europe (via Baltic)' which bring together stakeholders from politics, business and academia are promising steps to make progress on issues such as nonstop trans-shipment, one document service and a one stop

information system.

But without Chinese investment in manufacturing in the BSR, the China-Europe cargo rail transport and further multimodal transport and logistics development are unlikely to contribute sufficiently to closing or even significantly narrowing the growing trade deficit BSR countries run with China.

#### **Attracting Chinese investment while maintaining the BSR's long-term competitiveness**

The OBOR initiative is set to facilitate China's ongoing economic transition from an export- and inbound foreign direct investment (FDI)-led growth model with previously double-digit GDP growth rates to a more sustainable economic model (the so-called 'new normal') with lower growth rates of 6 to 7% which is more strongly based on domestic consumption, services and innovation. This opens a wide range of business opportunities for BSR countries to diversify their trade and investment partners and bring to bear their know-how in the fields of agro-food technologies, advanced manufacturing, innovative city designs, health care, and green technologies to name just a few.

Chinese FDI is highly welcome in BSR countries, as it may boost domestic growth, create jobs and opportunities for BSR companies to tap into the large Chinese consumer market. However, at least two interconnected challenges arise in this context: first, the need to align China's ambitious industrial policies with the interest of BSR countries in maintaining long-term competitiveness which is supported by EU policies, including the EU Baltic Sea Region Strategy, and EU funds, and second, the lack of unrestricted access for BSR companies to the Chinese market. In the absence of the EU-China comprehensive agreement on investment (CAI) which is still under negotiation and next to investment protection will include crucial market access provisions there is no level playing field. This asymmetric situation may easily be leveraged by China in bilateral relations with BSR countries.

By pursuing its OBOR initiative China seeks to integrate deeper into Asian, African and European value chains through regional integration which has partly been conceived as a replacement strategy for China's exclusion from the Trans-Pacific Partnership (TPP). To speed up its economic upgrading and to avoid falling into the middle-income trap, China needs to acquire advanced technologies which are so far concentrated in Europe, Japan, and North America. China's path to world leadership in a number of key technologies is outlined in the 13th Five Year Plan (2016-2020) and notably in the 'Made in China 2025' strategy which has taken inspiration from Germany's Industry 4.0 strategy that seeks to integrate information and manufacturing technologies for intelligent manufacturing.

The Berlin-based Mercator Institute for China Studies (Merics) has analyzed China's Made in China 2025 strategy and the recent

series of takeovers of German high technology companies such as the robotics firm Kuka by Chinese companies. Merics has identified potentially adverse implications of this strategy for industrialized countries and has provided a number of policy recommendations. These appear to be highly relevant for BSR countries which host high technology industries and are likely to be the privileged future targets of Chinese investors such as the Nordic-China Growth Fund, a private equity fund set up by state-owned Beijing Capital Investment, which focuses on companies involved in clean technologies, health care and advanced production technology.

According to media reports, the fund seeks to support companies located in Nordic countries to enter the Chinese market. In return the companies concerned would need to transfer intellectual property rights (IPRs) to a joint company established in China which would benefit from the innovations developed by Nordic countries in mainland China and other parts of Asia. According to this logic, the restricted access for BSR companies to the Chinese market among others under the Catalogue for the Guidance of Foreign Investment Industries would be used by Chinese companies as a bargaining chip to acquire state-of-the-art technology from BSR companies, while Chinese companies profit from the BSR's liberal investment regimes based on free market principles.

China's state-led 'business model' and its industrial policies guiding the behaviour both of state-owned enterprises, which still account for the bulk of Chinese FDI, and private companies may lead to China absorbing advanced technologies of BSR countries on a large scale. This may result in short- and/or mid-term commercial gains for BSR companies due to better access to the Chinese market. In the mid- to long-term, however, BSR companies may be edged out from the Chinese market and third countries' markets by their Chinese peers supported by financial government backing BSR companies do not enjoy, as they operate under EU state aid, merger and public procurement rules aimed to guarantee fair competition. This potential evolution is

likely to be accentuated by the increasing gap in resources being devoted to research and development in Europe and China.

High-speed rail construction is a case in point. In this field China has within a few years gained technological proficiency based on technology transfers from Western companies. Research by the London-based Lau China Institute shows that with a combination of highly flexible 'lending-building' packages which condition the granting of soft loans from China's policy banks on the involvement of Chinese companies in construction work China Railway Rolling Stock Corporation (CRRC) has been able to out-compete its Western peers in almost all cases of OBOR-linked infrastructure construction. Economic viability of projects is only one factor among others in a strategy which appears to be aimed at landing contracts at almost any price to secure a foothold in new markets.

Against this background, it seems vital to ensure through appropriate policies that the envisaged OBOR-induced increase in trade volumes and investment flows, as well as infrastructure projects between China and the BSR – as coordinated through the EU-China Connectivity Platform – generate a genuine 'win-win situation' on a short- and long-term basis. ■



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# Gauging the impact of China’s One Belt, One Road Initiative on the Baltic Rim

Expert article • 2160

Most in the shuffle of political regime changes that dominated the public policy discourse of 2016 was a steadily rising tide of support for a potentially game-changing infrastructure program on the Eurasian continent. Referred to by a bevy of titles, China’s “One Belt, One Road” (OBOR) initiative will result in vastly improved land and maritime connections. Moreover, it will leave a host of large-scale infrastructure development projects peppered throughout the continent in its wake. This once-in-a-generation type of imperial infrastructure investment is on par with the development of the British railroad network in the 1800s and the Marshall Plan of the 1940s. Whereas the Marshall Plan was estimated to have cost \$130 billion in current US dollars, the OBOR’s price tag is estimated by the Chinese government to exceed \$4 trillion.<sup>1</sup> If this project is fully realized, it will travel through a staggering geographic area: upwards of 60 countries stretching from eastern China through Central Asia and ending in Europe. The Baltic Sea region must take note of this changing landscape and coordinate home-grown infrastructure development programs that allow it to capitalise on these new investments and pivot towards China.

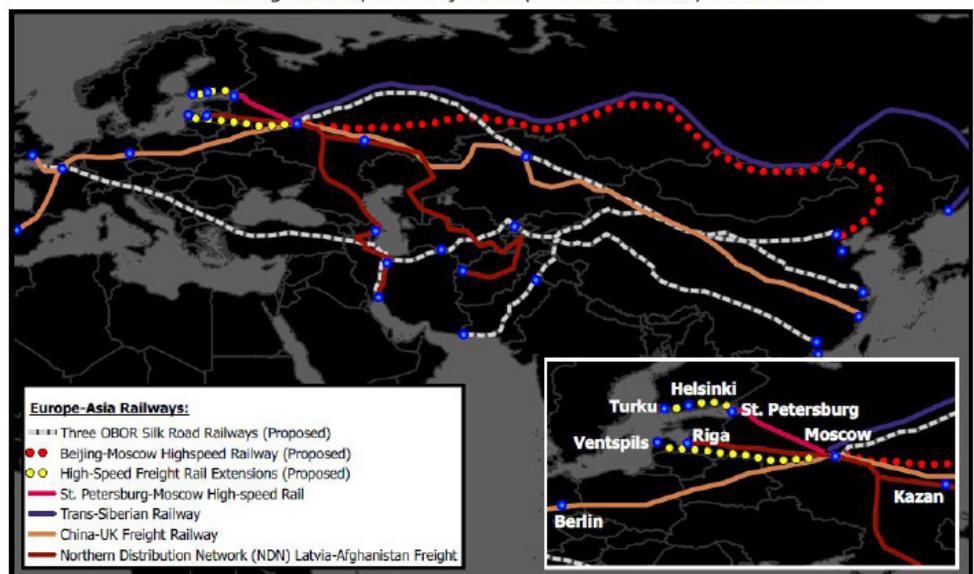
Enthusiasm for the potential of China’s flagship infrastructure project is high in certain parts of Europe, specifically Eastern and Southern Europe. While Western Europe has been hesitant to hitch their wagon to China, much of Eastern Europe has already cozied up to China. The “16+1 Initiative” was spearheaded by China in 2012 to increase cooperation in the areas of infrastructure, high-tech industries, and green technologies with eleven of the eastern-most EU states and five Balkan countries. The three Baltic countries, especially Latvia which coordinated its 2016 conferences, have been ardent supporters and facilitators of this cooperative initiative with China. The result of this coordination has been numerous high-level conferences and white papers on the subject of Chinese-European coordination. Meanwhile, Western Europe and the Nordics have tip-toed fairly cautiously when discussing China’s ambitious investment plans. Until recently, Europe was committed to the wide-sweeping transatlantic trade deal, TTIP, with the US. With that trade-deal effectually

dead on short and medium term, Western Europe must awaken to the new reality of China’s increasingly ambitious infrastructure investment scheme.

At the same time, there are other transportation infrastructure investment initiatives in the region in addition to the OBOR. Russian officials are currently seeking funding for its planned Moscow-Beijing high-speed rail line. Moscow recently announced that it will break ground on a \$17 billion first leg. This combination of Russian rail infrastructure upgrades and the OBOR suggests that the future of the region lies in connecting Asian markets with Russia through Moscow. Despite ongoing political tensions between the West and Russia, one question to be answered rather soon will simply be which country will become the preferred partner to connect Moscow with the EU.

An increasingly connected Beijing and Moscow brings seemingly infinite new opportunities to the region, but European leaders must proactively join this new wave of development. If Moscow becomes the effective western boundary of the Chinese hegemon, the possibility of connecting the Baltic rim to Beijing are now within grasp via one additional infrastructure project: the construction of a high-speed freight line connecting Moscow to Helsinki, Tallinn, or Riga. From a technical perspective, rail improvements with Moscow are entirely possible, since all three countries have 1520 mm gauge railway, a

Existing and Proposed Major European-Asian Railway Connections



<sup>1</sup> The Economist. “Our bulldozers, our rules: China’s foreign policy could reshape a good part of the world economy.” 2 July, 2016. Source: <http://www.economist.com/news/china/21701505-chinas-foreign-policy-could-reshape-good-part-world-economy-our-bulldozers-our-rules>

legacy of their shared history as a part of the Russian empire prior to WWI. These wide-gauge railways guarantee these countries' role as the western terminus of Chinese and Russian shipments, since train cars must otherwise carry out the burdensome and time-consuming task of unloading and reloading their goods onto 1435 mm train tracks when they reach Western Europe. Thus, with these technical considerations in common, the only factors deciding which country will become China's entry point into the Baltic rim are economics and political will.

Finland has several obvious advantages, namely its GDP, which is approximately three times that of Estonia and Latvia. It also has a well-developed high-speed rail system that extends to St. Petersburg. A new high-speed freight connection from Moscow to Helsinki could be extended to Finland's second-largest port in Turku, which could increase job opportunities in the region considerably. However, it cannot compete with the low labor costs of Estonia and Latvia have very competitive wage rates and relatively high labor productivity rates. Furthermore, their comparatively less-developed infrastructure yields greater potential rewards that could be gained from new investment in transportation and shipping.

Perhaps, the more intriguing play for increased freight rail linkages with Moscow would be Latvia. Riga's proximity to Moscow and relative proximity to East Asia in comparison to the rest of Europe are a clear asset. Furthermore, access to three Latvian ports, and access to well-established existing freight linkages position Riga as the preferred freight rail alternative to any other country in the Baltic Sea Region. The rail extension could also be stretched eastward a mere 180 kilometers to Ventspils, which has vastly underutilized shipping capabilities due to its history as one of the largest ports during the Soviet Union. Perhaps, the greatest advantage Riga has over Helsinki is its Russian linguistic prowess, since approximately half of the city's residents are native speakers and a much larger percentage of the city speaks with advanced fluency. This strategic and competitive advantage extends Latvia's trade capabilities beyond Russia into the booming Central Asian economies — the majority of which have experienced annual GDP growth rates exceeding six percent for the past five years — and would position Latvia as the prime gateway between Asia and Europe in a similar capacity to how Helsinki has become the passenger airlines gateway between the EU and China.

Politically, such a large-scale proposition will always be challenging but, at the very least, a further analysis of the financial feasibility of such a project is warranted, due to the massive scale of potential trade opportunities that are within grasp. The job opportunities that could potentially be created by an infrastructure investment of this size would consist of far more than just the temporary construction and project management jobs required to build the train lines. By extending China's effectual economic borders through Russia and onto EU soil, the country who reaches the finish line first and successfully lures imports from China's 1.4 billion-person economy will yield seismic impacts in terms of job creation. An enormous amount of high-paying logistics and shipping jobs await the victor, the likes of which could dwarf all other industries in the Baltic Sea region today. Furthermore, during a time of increased military tension in the region, something even greater could result from the cross-country coordination of this large infrastructure investment: demilitarization and peace. ■



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TAMAS MATURA

# China and Central and Eastern Europe: threat or opportunity?

Expert article • 2161

The cooperation project of China and its sixteen Central and Eastern European partner countries (Albania, Bosnia and Herzegovina, Bulgaria, Croatia, the Czech Republic, Estonia, Hungary, Latvia, Lithuania, Macedonia, Montenegro, Poland, Romania, Serbia, Slovakia and Slovenia) has been attracting a lot of attention since its birth in 2011, while it has created suspicions on the European level as well.

The so called '16+1' initiative has raised many questions regarding the true nature of the project, the intentions of the Chinese side and its potential impact on the integrity of the Union. CEE countries had to learn how important communication was, in order to convince European authorities that 16+1 was not a real threat to the common China policy of the EU.

When Beijing introduced the outlines of the cooperation between the Middle Kingdom and its sixteen Central and Eastern European partners in 2011-2012, most observers believed that China had a well prepared and detailed plan in the background. Since this supposed plan has never been published or even talked about, some people developed concerns regarding the true intentions of China. Was it to divide and rule Europe? At the same time CEE countries have been trying hard to figure out what Beijing wanted or needed to fit into the 'plan'. It had to be learnt that the Chinese way of thinking and communication was different from the Western style: Beijing follows the well-known East Asian tradition of inductive thinking, while the West tries to understand it through its deductive traditions. It means that countries with different traditions are suspicious about China's intention, because they think there might be a secret plan behind the curtain. Through the 16+1 cooperation it became clear that a proactive attitude should be adopted by participating countries to shape the project together with China.

When it comes to the results of the 16+1 time and patience plays a significant role, since the cooperation started only five years ago in Budapest. Governments have done a lot to make business circles aware of mutual opportunities, the legal and political framework has been established. Now it is up to entrepreneurs, tourists, students and scholars to walk their way through the myriad of new opportunities.

Of course, there are challenges as well. When it comes to investment issues, China and the CEE countries have diverging interests in many cases. While the region desperately needs green field investments and new jobs, China is more interested in infrastructure construction and financial cooperation. However, the One Belt One Road project of China may give even more substance

and content to the 16+1, since CEE countries are geographically predestined to be part of the new trade route. The looming project of connecting the port of Piraeus in Greece with Budapest through Macedonia and Serbia is one of the first examples of how OBOR and 16+1 may eventually merge together. Meanwhile China is considering to relocate some of its industrial or manufacturing capacities into foreign countries to rebalance its domestic economic structure and its foreign trade. Central and Eastern Europe is a region which might be able to attract such kind of Chinese investment, and transportation corridors of OBOR may offer a particularly good chance. Countries like Poland or Hungary are to develop proactive strategies to draw Chinese investors' attention to the potential business opportunities provided by their EU and Schengen Area membership.

However, besides the promising opportunities to individual countries, the Chinese activity has some concerning aspects when the pan-European perspective is taken into account. Beijing has attempted to establish a Nordic-Chinese (5+1) and a Mediterranean-Chinese (7+1) regional cooperation. That is, EU-China relations would be turned into a set of regional talks, while only major member states could keep their contacts with Beijing on a bilateral level. The 16+1

It had to be learnt that the Chinese way of thinking and communication was different from the Western style: Beijing follows the well-known East Asian tradition of inductive thinking, while the West tries to understand it through its deductive traditions.

cooperation is not a threat to the EU on its own, but if China succeeds to create a puzzle of regional forums across Europe, it is hard to see what role Brussels and the common China policy could play in the future. The potential proliferation of project like 16+1 across the EU is a concerning option, thus all member states and EU institutions should scrutinize the issue to articulate the proper strategy to the challenge imposed by the increased Chinese presence in Europe. ■

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MICAEL BLOMSTER

# New Scandinavian rail hub for China traffic over North Finland

Expert article • 2162

In the past years, the rail bridge between China and Europe across Russia became an economic option – faster than sea, cheaper than air. A look at the globe shows that rail has specific advantages in the Baltic Sea area, where a short rail link competes with a long sea route. RailGate Finland of Kouvola town, at the route between Helsinki and St. Petersburg, goes for the Scandinavian hub function as a business model.

Kouvola RailGate Finland is boosting the efficiency of the Scandinavian-Mediterranean Core Corridor (ScanMed Corridor) as well as the flow of goods beyond Mediterranean, all the way to the Asian growth markets. The main bottlenecks identified within the ScanMed – Asia corridor are now solved with a signed agreement between ScanMed – Asia corridor transport actors from China, Kazakhstan, Russia and Finland in December 2016. During the first part of 2017, new test trains are to be launched in the ScanMed – Asia corridor, and soon after completed tests, a regular weekly-base train connection will start to operate.

Director Simo Päivinen from Kouvola Innovation Ltd., a member of the Open ENLoCC Network, proudly says “after intensive preparations it is now our great pleasure to introduce for the North European export industry a new route to Asia, and it is namely the shortest train route connection from European borders to Asia. This new option is positively affecting to the functionality of many other European and international corridors”. Päivinen continues: “This corridor opening is also aimed to ecofriendly, clean fuel transport development, including advancing smart telematics applications for efficient infrastructure use and for better integrating many rail freight movements. It is prime time to move towards a competitive, resource efficient and eco-friendly transport system as guarantee for efficient business infrastructures and ensuring accessibility and connectivity for all regions with secure and sustainable logistics systems”.

Päivinen states, “I personally think that it is now highest time to stop talk about the Europe – Central Asia railway transport connection as expensive, time-consuming and not flexible for customers’ needs. We are focusing to change this image of train transport as well as multimodal freight operations with a combined utilization of new smarter and efficient logistics. For the transport volumes of international corridors, we are creating a new type of rich customer base, which is basis for the future volume growth of multimodal transports in the corridors between North Europe and Asia.

The main event of this corridor development and follow-up, **Kouvola Rail Forum 2017** (September 28), is foreseeing a new impetus and take-up of well-functioning international transport corridors and their next key position in the processes of creating successful and efficient transport system and structures in the future world. Well cooperation between countries and continents are really needed in the up-coming years when moving towards sustainable logistics and ecofriendly international transport.

## New Northern Scandinavian rail hub - Tornio/Haparanda

In the end of 2016, businessman Micael Blomster was in contact with Director Simo Päivinen concerning an idea about the railway connection from Asia. How realistic was the idea that the connection could continue up to North Finland and to Sweden.

Their co-operation gained an idea to an achievable and realistic thought of that the railway connection between Scandinavia and Asia could be expanded up to Tornio / Haparanda region, where the only railway connection between Finland and rest of the Nordic countries exists. This idea got a work name as “New Silk Road”.

Blomster says that the whole idea generated large interest when he took contact with municipalities in region. In the middle of December 2016 each of parts had a meeting in the region. Next meeting will be a bigger Seminar in Tornio/Haparanda region together with municipalities and different company organisations. The purpose is to investigate what the new China traffic could bring to the region.

One thing is clear, a new logistic center for re-loading needs to build up in the region, but what else is needed, is a question for the Seminar to find out. ■



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KARI REINIKAINEN

# Chinese yards to challenge Europe in passenger ship building

Expert article • 2163

**E**uropean builders of passenger vessels - cruise ships and ferries - have had concerns about the prospect of competition from builders in the Far East since at least the 1980s. However, relatively little has happened so far: efforts by Japanese and South Korean shipbuilders to establish themselves as exporters of passenger ships have produced only short term successes of limited scale.

However, shipbuilders in China are now looking into this business as well and it they appear to have adopted a different strategy than their peers in the region by teaming up with a major European builder and the world's largest cruise ship operator. This strategy involves a lower risk than that adopted by the Japanese and Koreans and it may play a decisive role between success and failure.

Major shipyards in the Far East mainly build commodity vessels - dry bulk carriers, oil tankers and container vessels. These are often standard designs of the yard and steelwork accounts for a lions' share of the work. Passenger vessels are mainly built to the design of the owner and fitting out is the major part of the work, both in terms of cost and time. Good project management skills are of vital importance in a successful passenger ship building project.

## Japan - home market failed to provide lift for exports

Japan has a substantial network of ferry services and until the rise of China, it was also the principal source of cruise passengers in Asia. The domestic ferries are built on local yards and at the turn of the 1980s to 1990s, a number of cruise ships were also built to cater for the domestic market. In 1990, Mitsubishi Heavy Industries delivered Crystal Harmony to Crystal Cruises, then owned by Nippon Yusen Kabushiki Kaisha (NYK) that served the top end of the Western market.

About a decade later, the same yard won an order from Princess Cruises to build two 116,000 gross ton ships for Princess Cruises. However, the first vessel caught fire while being fitted out and was actually delivered a year late. This was a bitter blow and only in 2011 did the company sign another cruise liner contract, with AIDA Cruises in Germany.

This was for two 125,000 gross ton vessels of a completely new design with some novel technical features. The complexity of the project meant that work soon fell behind schedule and started to exceed budget. The first vessel entered service in 2016 and the second one is due in the summer of 2017. Mitsubishi booked massive losses from the project and decided not to seek further work in cruise ship building.

## South Koreans' efforts bear some fruit in ferry but none in cruise ship building

Shipbuilders in South Korean managed to establish themselves as builders of several large and fast ropax ferries with overnight accommodation to customers in Europe, mainly in the Mediterranean region, at the turn of the millennium.

Unfortunately for them, the ferry sector in Europe did not enjoy a similar period of strength as the cruise sector did in the years before the financial crisis, and even after that. Investment in new tonnage remained limited until about 2015, when sharp fall in the price of oil improved ferry operators' profitability and convinced many of them to proceed with plans to replace ageing vessels with newbuildings.

So far, South Korean yards that have suffered badly from a sharp fall in the orders for commodity type ships that accelerated in 2016, have not been able to win export orders from European ferry companies. They have not built a single cruise ship.

## China - strategy of cooperation can fill technology gaps and ensure success

That the Chinese are serious about entering cruise ship building was made clear in late 2014, when China State Shipbuilding Corporation (CSSC), the Italian shipbuilding group Fincantieri that is the world's biggest builder of cruise ships and Carnival Corporation & plc, the Anglo-American group that is the world's largest cruise operator, signed a joint venture agreement to develop cruise ship building in China.

In the following autumn, Carnival plc, the British holding company in the Carnival group, formed a joint venture with China Investment Corporation to establish a cruise brand for the Chinese market. Finally, in the autumn of 2016, the yet unnamed venture ordered two 133,500 gross ton ships from CSSC, with an option for two more.

The first joint venture secures technology transfer that is important as CSSC has no previous experience from building cruise vessels. The gross tonnage of the vessels the Carnival led joint venture ordered suggests that these will be based on the Carnival Vista class, which Fincantieri has on order for two existing Carnival group brands. In other words, it has experience from building ships of this class at home in Italy.

CSSC will have to set up a network of suppliers and contractors and at least initially, many of these will have to come from Europe. Finding ones may be difficult due to high workload at European cruise ship builders, but due to their experience in the sector, Europeans are valuable partners. Project management is another key challenge to a builder inexperienced in the sector, but here Fincantieri's assistance will probably be available and it may well be crucial.

### Chinese builders have won orders from Europe

In the ferry sector, a Chinese yard is building two, fast LNG powered ropaxes for Rederi AB Gotland in Sweden. These vessels will not have cabin accommodation, but they are the second batch of ships the Swedish company is building in China.

Stena Line, a major Swedish company, has contracted the AVIC shipyard in China to build up to eight large ropax vessels. AVIC is the principal shareholder in Deltamarin, the Finnish consultant naval architects, with in depth experience in the passenger ship sector. The acquisition itself can be seen as evidence of the Chinese to establish themselves in passenger vessel construction.

The most prestigious ferry order a Chinese yard has won from the West is for a 63,000 gross ton cruise ferry Viking Line, the Finnish cruise ferry company, intends to build at Xiamen in China. While ropax vessels tend to have functional but not luxurious accommodation, cruise ferries are usually fitted out to much higher specifications in terms of passenger facilities. Deltamarin will be involved in this project as well.

It is unlikely that shipbuilders in China will even attempt to win an export order for a cruise ship from a major operator in the west until they have successfully completed at least one vessel for the domestic market as a proof of their capabilities.

In the ferry sector, however, the situation is different. These vessels are less expensive and less technically demanding than cruise ships. Many ferry companies in northern Europe in particular operate aged tonnage and Chinese builders are likely to continue to work hard to win further contracts in this sector. They will probably offer longer delivery times than an established European builder, but to compensate for that, even a significantly lower price. ■

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# BALTIC RIM ECONOMIES

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OTT KOPPEL

# Some side notes about Rail Baltic

Expert article • 2164

**R**ail Baltic is a 1435 mm gauge railway line from north to south that would connect Scandinavia with Western Europe. The implementation of the project is expected to take place during the years 2018/2019...2025 in cooperation between the Baltic countries and with the participation of Finland and Poland. The total length of the envisaged line would be ca 700 km and the driving speed for passenger trains up to 240 km/h and for freight trains up to 120 km/h. The preliminary cost estimation of the project amounts to ca 4.8 billion euros from which Estonia would need to cover ca 1.3 billion. Close to 80% of funding is applied for from the Connecting Europe Facility (CEF) from which 442 million euros was already allocated in summer 2015 (sums without own contribution).

In summer 2011, the Government of Estonia decided to build the section of Rail Baltic located in Estonia (229 km) on a completely new direct route passing through Pärnu. No other railway connections are planned to be constructed between Estonia and Latvia. Therefore, the plans envisage that Estonia will have a railway network with two different gauges in the situation where the volumes carried on the existing lines have been decreasing and there is a shortage of financing for network maintenance. The main justification of the project i.e. short travel time to Riga and other European destinations is valid only for the residents of Tallinn and Western Estonia, whereas, according to the national planning policy statement Estonia 2030+, the area serviced by the 1520 mm railway lines covers the area of inhabitancy of ca 80% of Estonian residents.

The nature of freight planned to be hauled on the Rail Baltic line raises questions which are amplified by the results of a recent tender for the analysis of technological and spatial needs of the Muuga multimodal terminal. Meanwhile, there already exists an intermodal terminal with unused capacity in Muuga. The economic relations between Rail Baltic and Tallinn-Helsinki railway tunnel (Talsinkifix) are yet to be determined. The Estonian public opinion (e.g. the association Publicly about Rail Baltic) has pointed out also other discrepancies of the project which may partially be caused by lack of communication on behalf of the Ministry of Economic Affairs and Communications and Rail Baltic Estonia Plc. The debate has focused also on the circumstances related to the construction project, such as planning, movement of animals, lack of necessary construction materials, etc. Meanwhile, it has remained unclear for the author of the present overview what are the sources for covering the annual operating and capital costs of Rail Baltic.

Until the end of the 2016/2017 traffic timetable period, the railway infrastructure access fee is calculated in Estonia (and with certain specific features also in the other two Baltic countries) using the fully-distributed cost (FDC) method and the infrastructure management full costs include direct and indirect operating costs, capital cost (in the meaning of depreciation) and so-called reasonable business profit (the weighted average cost of capital multiplied with the net book value of fixed assets). The basis for calculating train kilometre and gross tonne kilometre unit cost differ in case of the two Estonian railway infrastructure managers (Estonian Railways Ltd and South-Western Railway Infrastructure Ltd) but as a general principle, in case of applying this method the users cover all costs related to the use of

railway. Nevertheless, as the volumes carried on the Estonian railway network have dropped drastically, the price caps determined in the respective methodology force the government to compensate the revenue not earned by railway infrastructure undertakings to a certain extent already now.

Starting from the 2017/2018 traffic timetable period, Commission Implementing Regulation (EU) 2015/909 (on the modalities for the calculation of the cost that is directly incurred as a result of operating the train service) for the Directive 2012/34/EU of the European Parliament and of the Council (establishing a single European railway area) will be implemented in Estonia. The implementing regulation stipulates that the cost of the minimum access package provided to the rail transport undertakings is based on the direct costs related to the organisation of train traffic that do not include such costs as overheads and other costs of permanent nature (incl. depreciation), as well as financing costs. The total share of such costs in the full cost of railway infrastructure management amounts according to various estimates to 70-80%.

The potential harmonisation of railway infrastructure user fees across the Baltic countries could be regarded as a positive change stemming from the review of railway infrastructure pricing model. Meanwhile, the arguments of the Estonian Ministry of Economic Affairs and Communications that the running costs of Rail Baltic will be fully covered by its users are certainly not true. Although the legislative acts mentioned in the previous section do not exclude the possibility to apply mark-ups for full or partial coverage of fixed costs, the government has still the obligation to prove the solvency of market.

Whilst comparing the initial estimates for the current expenditure (in Estonia ca 30 million euros per annum) and potential (but unreasoned) volumes (10...16 million tonnes), we can assume based on the existing experience that there would be a significant deficit of resources for covering the costs of the railway infrastructure manager. The author is not aware of any relevant compensation mechanisms in the financial forecasts of the government and we should also not forget the need to maintain the already existing railway network. In addition, the need to accumulate resources for the renewal of the new railway line will rise during the 20-40 years after the completion of the project.

Hopefully, the detailed cost-benefit analysis to be completed by Ernst & Young in March 2017 will remove any doubts but until then the economic justification of Rail Baltic remains unconvincing. ■

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HILTGUNT FANNING

# The economic development of the Baltic Sea Region<sup>1</sup> - what major indicators tell us

Expert article • 2165

Early in the 1990s, when the Berlin Wall had come down, enthusiasm about the perspectives for the future was unbridled in the Baltic Rim countries. Old ties were strengthened, new plans made, networks created, projects initiated, and numerous organisations from governmental to local levels founded within just a few years.

And, indeed, for more than fifteen years, the Baltic Sea Region developed at high speed, the Baltic states (Estonia, Latvia, Lithuania) and Poland joined the European Union, and the Baltic Sea Region was deemed "one of the most dynamic economic areas of Europe."

At the same time, however, the region's prosperity remained below peer regions; and analysts repeatedly pointed at performance imbalances between member countries and improvement needed regarding different aspects of economic performance, such as GDP, competitiveness, digitalization, employment, inflation, sustainability, or wealth.

For gaining a clearer picture of the BSR's economic performance since the mid-2000s, two types of data were considered: firstly, the traditional macro-economic indicators of GDP, GDP per capita and FDI, and secondly, more modern indices/rankings, viz. the *Global Competitiveness Index*, the *Ease of Doing Business Index*, the *Economic Freedom Index*, the *European Innovation Scoreboard*, the *World Investment Report*, the *Global Cleantech Innovation Index*, and the *Networked Readiness Index*.

## GDP and GDP per capita

The below table lists the values of the 10 BSR states, the overall performance of the region, the values of the European Union and of the United States.<sup>2</sup>

<sup>1</sup> The term Baltic Sea Region here includes the nine countries adjacent to the Baltic Sea (Denmark, Estonia, Finland, Germany, Latvia, Lithuania, Poland, Russia, Sweden) and Norway due to its proximity to the Baltic Sea, to its long historical ties to the other countries of the region and to its shared land borders with three of them.

<sup>2</sup> All values were taken from the CIA World Factbook.

COUNTRY / REGION	Year	GDP (PPP est.) USD billion	per capita (USD)
Denmark	2005	188.1	34,600
	2010	201.7	36,600
	2015	257.4	45,800
Estonia	2005	22.3	16,700
	2010	26.7	19,100
	2015	37.9	28,700
Finland	2005	161.5	30,900
	2010	186.0	35,400
	2015	224.7	41,200
Germany	2005	2,504.0	30,400
	2010	2,940.0	35,700
	2015	3,842.0	47,400
Latvia	2005	30.3	13,200
	2010	32.5	14,700
	2015	49.8	24,500
Lithuania	2005	49.2	13,700
	2010	56.6	16,000
	2015	82.1	28,000
Norway	2005	194.1	42,300
	2010	255.3	54,600
	2015	352.8	68,400
Poland	2005	514.0	13,300
	2010	721.3	18,800
	2015	1,003.0	26,400
Russia	2005	1,600.0	11,100
	2010	2,223.0	15,900
	2015	1,236.0	9,243
Sweden	2005	268.0	29,800
	2010	354.7	39,100
	2015	467.4	48,000
BSR as a whole	2005	5,531.5	23,600
	2010	6,997.8	28,590
	2015	7,553.1	36,764
EU	2005	12,180.0	28,100
	2010	12,790.0	33,596
	2015	19,180.0	34,861
USA	2005	13,090.0	44,308
	2010	14,960.0	48,377
	2015	17,950.0	55,800

As can be seen, all Baltic Rim countries - except Russia - exhibit continuous growth; and in 2015 the BSR GDP per capita average exceeded the EU average. This good result loses its lustre, however, when compared with the US performance and a gap of about 50%. But even within the BSR, the long-standing East-West divide is still present, although it has narrowed somewhat – in 2005, the GDP per capita average of Estonia, Latvia, Lithuania, Poland, and Russia amounted to 38% of that of Denmark, Finland, Germany, Norway and Sweden; and in 2015 it amounted to 46% (54% if one excludes Russia's performance).

### Competitiveness

The **Global Competitiveness Index** compiled and published by the WORLD ECONOMIC FORUM is a cross-country benchmarking analysis of the factors and institutions that are perceived as determining long-term growth and prosperity.

While in 2005, four BSR countries (Denmark, Finland, Germany, and Sweden) made it into the Top 10 group (with Norway on rank 12 being close), whereas the positions of Estonia (25), Latvia (36), Lithuania (40), Poland (48) and Russia (62) were far behind – with a BSR average of 24; in 2016, it was Germany, Lithuania, Norway and Poland that had improved their performance, whereas all other BSR member states had lost ground, with the BSR average being 22.5, a very modest improvement.

### Ease of Doing Business

The *Ease of Doing Business Index* compiled by the WORLD BANK ranks economies regarding ten factors that contribute to a business-friendly environment conducive to the starting and operation of local firms., such as starting a business, obtaining construction permits or getting electricity.

The performance of the Baltic Sea Region in 2016 was as follows: Denmark – rank 3 (from 8 in 2005), Estonia – rank 12 (from 16 in 2005), Finland – rank 13 (stable compared with 2005), Germany – rank 17 (up in performance from 19 in 2005), Lithuania – rank 21 (15 in 2005), Latvia – rank 14 (26 in 2005), Norway – rank 6 (rank 5 in 2005), Poland – rank 24 (an impressive improvement from 54 in 2005), Russia – rank 40 (up from 79 in 2005), and Sweden – rank 9 (up from rank 14 in 2005). The BSR average moved up nearly 10 ranks from 25 in 2005 to 16 in 2016; and gaps between the best performers and countries on lower ranks are narrowing.

### Economic Freedom

The *Index of Economic Freedom* measures the impact of liberty and free markets on economic freedom and progress. Factors considered include e.g. property rights, freedom from corruption, fiscal freedom, labour freedom and monetary freedom.

In this index, only five BSR countries (Denmark, Estonia, Germany, Lithuania and Poland) have been able to improve their ranks compared with 2005; the ranks of Finland, Latvia, Norway, Russia and Sweden, on the other hand, deteriorated (Russia even fell back from rank 102 to rank 153; while Latvia only changed from rank 35 to 36).

### Innovation

For detecting trends regarding innovation, two sources were used – *The European Innovation scoreboard/Innovation Union Scoreboard* and the *Global Cleantech 100 List*.

The **European Innovation scoreboard/Innovation Union Scoreboard** (since 2011) is an instrument of the EUROPEAN COMMISSION, developed under the Lisbon Strategy to provide a comparative assessment of the performance of EU Member States.

According to the 2016 Scoreboard, Denmark, Finland, Germany, and Sweden are Innovation Leaders with innovation performance well above that of the EU average. Austria, Belgium, France, Ireland, Estonia, Latvia, Lithuania, and Poland, on the other hand, are only Moderate Innovators with a performance below that of the EU average.<sup>3</sup>

Apart from the BSR being divided into two categories, the comparison of the values for 2008 and 2014 shows an improvement when 2008 is taken as the base year for all EU BSR countries except Finland, but a deterioration when 2015 is compared with 2014 for all countries except Denmark, Poland, and Sweden.

The **Global Cleantech 100 List** is a biennial report compiled by CLEANTECH GROUP. In it 100 companies (chosen from several thousand) are presented, which are seen as best-positioned to solve clean technology challenges and to disrupt the markets they innovate in.

Assuming the assessment is unbiased, the figures are sobering. In 2010, the United States can boast 54 companies in this list, the figure for the entire BSR amounts to 14, and Estonia, Latvia, Lithuania, Poland and Russia are not represented at all. But in 2015, the situation has even worsened – only 9 BSR companies are included, whereas the US figure has risen to 57.

<sup>3</sup> Since Norway and Russia are not members of the EU, their performance is not included.

### Information and Communication Technology

Analyses of economic performance frequently address the issue of how well-prepared economic actors are for the IT-driven *Fourth Industrial Revolution*.

An index measuring how well an economy is using information and communications technologies to boost competitiveness and well-being is the WORLD ECONOMIC FORUM's **Networked Readiness Index**.

Here, the BSR performance is much more satisfactory, not only because the values have improved noticeably, but also because the gap to the United States is shrinking. In 2010 the BSR average was 4.71 (with the maximum value possible being 6.0), whereas the USA value was 5.33. In 2016, the BSR value was 5.30 versus 5.8 (USA).

### Investment

To gauge performance regarding attractiveness to investors, information in UNCTAD's *World Investment Report* was utilised to calculate FDI inward stock per capita for the BSR and compare it with that of the USA. Unfortunately, the results are thoroughly satisfactory only for Denmark, whose figures (2010 – 2015) have grown and are better than the USA's. Norway's and Sweden's figures both in 2010 and 2015 are better than those of the USA, but they are lower in 2015 than in 2010.

### Conclusion & Suggestions

- 1) The BSR overall economic performance has not developed as well as we had hoped.
- 2) The East-West divide in performance is still in existence.
- 3) Russia's figures in most categories give reason for special concern.
- 4) While the intra-European comparison is acceptable, the global perspective highlights BSR shortcomings.
- 5) Hence, we need to rekindle the enthusiasm of the early 1990s to cope with the current and future challenges and all efforts need to be made to create a novel perception of unity in the BSR.
- 6) Various suggestions presented in articles in the *Baltic Rim Economies*, should be picked up and implemented, e.g. a common BSR innovation strategy or a BSR media channel. ■



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# The impact of EU's sanctions on Russia and Russia's counter-sanctions on Finland's exports to Russia

Expert article • 2166

The European Council decided in December 2016 to extend the economic sanctions against Russia until 31 July 2017. Initially these sanctions were taken into use in July 2014 due to the Ukrainian crisis. Access to EU capital markets was limited for major Russian state-owned financial institutions. In addition an export and import ban on trade in arms was introduced as well as an export ban for dual-use in goods for military use in Russia. Exports of technologies and services from EU to Russia that can be used in oil production and exploration have also been restricted.

Looking at international trade statistics one can find out some facts about exports of the banned products to Russia. First we can take a look at the nine commodity groups which are part of product class CN-7304. These products are used for oil or gas pipelines and in drilling for oil or gas. It seems that it is quite difficult to draw any strong conclusions from the statistics as the total value of exports to Russia has varied a lot from year to year during the time period 2011-2015. From 2014 to 2015 the exports from Austria, Italy, France and Germany to Russia have however decreased substantially. It is very likely that the reason is the sanctions on Russia, but based on the statistics for such a short period of time it is impossible to tell for sure as there can also be some other reason.

As regards the ten banned product groups in the section CN 7305-7306, line pipes used for oil or gas pipelines, there are very few EU countries which have been exporting to Russia, even before 2014. The impact of EU's sanctions on Russia in these groups is thus very small. Singapore and Japan are major exporters to Russia in one of the forbidden product groups. In another group Ukraine has been a major exporter until 2015. Only once, in 2011, Finland was a major exporter in that group. Also Germany and Japan had big deliveries in 2011. In a third commodity group the United States of America is the major exporter to Russia.

There are two product groups in the CN-8207 category, the exports of which are restricted. The major exporters of rock-drilling and earth-boring tools to Russia are the United States of America, China, Sweden, India, Germany, Singapore, Canada, Mexico, India, Belarus and Finland. The non-EU countries are the most important ones for Russia in this category.

In the product class CN-8413 there are fifteen commodity groups including different kinds of hydraulic pumps, the exports of which are restricted. Germany, China, the United States of America and Italy are the biggest exporters of these products to Russia. The exports from Germany were very stable during the years 2011-2014, but declined substantially in 2015. The most probable reason for the decline is the sanctions on Russia. However, also the exports from China

decreased in 2015, but not as much as the German exports. Total exports to Russia of these fifteen product groups decreased already in 2013 as the exports from the United States of America fell steeply, but a moderate increase in US exports was seen in 2015. Exports from Italy declined in both 2014 and 2015.

World exports of boring and sinking machinery for boring earth or extracting minerals or ores to Russia, was very high in 2015 as it tripled from 2014. The exports from Germany were unusually low, but on the other hand exports from Italy were very high. More than half of the products came from China.

German exports of machinery parts in the four subgroups of CN-8431 stayed at the same level in 2015 as in 2014. Italian exports, however, were exceptionally high. As comes to mobile drilling derricks EU is only a minor supplier. This also concerns floating or submersible drilling or production platforms and other vessels.

On the basis of the trade statistics, there's no clear sign that EU's sanctions on Russia would have had any greater negative impact on the EU countries' exports to Russia. Further analysis is needed in order to be able to make more definitive conclusions. As regards Finland the value of exports of goods mentioned in the sanction list set by the EU is very low so the negative effect is almost negligible.

Russia's counter-sanctions towards food exports of the dairy and meat industries have however had a much greater negative effect on Finland's exports. The share of the sanctioned product groups of Finland's total exports to Russia (all branches) was about five per cent during the years 2010-2013, but in 2015 the share was only 0.09 per cent. The share of dairy products and cheese in Finnish food industry exports to Russia was 60 per cent in the year 2013 and still 53 per cent in 2014. As a consequence of Russia's import ban the share was only 0.9 per cent in 2015. Before the sanctions Russia's share of Finland's food industry exports was about one third, but in 2015 the share was only 8.6 per cent. ■



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# Sanctions: no pain, no gain

Expert article • 2167

**S**anctions, one of the favourite foreign policy tools practiced by US and, consequently, EU. What are economic sanctions in international relations? I am not a political expert, but let me provide a view from economist's perspective. Sanctions are restrictions for operations between sanctioner and sanctionee aimed to cause damage to sanctionee in order to force sanctionee to act in the way that sanctioner finds proper. If sanctionee's economy is somewhat big enough and able to sustain in a more or less long term, and if sanctionee is able to cause some economic damage to sanctioner then it is very likely to respond with counter-sanctions rather than concede. That is the way the 'sanctions war' unfolds. Economic sanctions could cause damage to sanctioner even without counter-sanctions response. Economic relations by its nature are beneficial for both sides, and the benefit is lost for the both if relations are suppressed.

So, in order to gain a result a sanctioner should not only cause pain to sanctionee but probably also suffer some pain by itself.

'Sanctions war' between US and EU on one side and Russia on the other side began in 2014,

Ukraine being the subject of the conflict. Putting aside the details, the sanctions imply that an access to international financial markets is severely restricted for Russia, and cooperation in the oil and gas sector is banned. Russia responded with ban for food imports from sanctioner countries.

The impact of sanctions on Russian economy is widely recognized as significant since its GDP has fallen by 3% in 2015 and 1% in 2016. Former US President Obama even claimed western sanctions have left Russia's economy "in tatters". However, the unbiased analysis shows that Russian economic problems were largely caused by drastic oil prices fall and corresponding devaluation of Russian exports rather than sanctions. According to forecasts by all international expert organizations Russia's GDP will rise by 1% in 2017. The recent privatization of Rosneft within which the 19.5 percent share of the biggest Russian oil company was acquired by foreign investors is yet another evidence that Russia has adapted to a new reality.

Russia's food embargo introduced as counter-sanctions has external and domestic aims. The external aim is obviously to respond properly to sanctions. The domestic aim is to legitimately protect national agriculture and food sectors. Food embargo was a great opportunity for Russian farmers to rapidly expand market share previously occupied by inexpensive European products. Statistical data on domestic food production shows that Russian agriculture sector has taken advantage of this opportunity. Physical volume of meat production in Russia has increased by 10% for two years, production of cheese has boosted by 30%.

Russian counter-sanctions directly impacts EU food exports. According to Eurostat, food and drinks exports to Russia has decreased by € 6 billion in 2016 as compared to 2013. Although total

food and drinks exports from EU have risen by € 10 billion for the same period. The best buyers who have increased purchases the most are China and United States.

Ban for cooperation in oil and gas sector and rapid fall of Russian currency rate has led to reduced machinery supplies to Russia. Machinery and transport equipment exports from EU to Russia have lost much more than food exports – the decrease accounted to € 25 billion. At the same time, thanks to increase in exports to United States by € 38 billion and other countries the total machinery and transport equipment exports from EU increased by € 30 billion.

During the 'sanctions war' EU total exports have slightly decreased, but the reasons for that lie outside EU sanctions or Russian counter-sanctions. EU has successfully extended foreign markets for export goods that are no longer welcomed in Russia or

banned to sell to Russia. The other side of the coin is that EU exports became less diversified in terms of partners. United States and China have grabbed share in EU exports left by Russia. EU export operations are now more dependent on these two superpowers,

though that could hardly be considered as a severe negative effect of the 'sanctions war'.

Russia has adapted to sanctions. National financial sector and oil and gas producers experience inconvenience, but do not show any signs of degradation. Moreover, Russian farmers pray for sanctions continuation. Current sanctions and counter-sanctions do not cause any unbearable pain to either party and do not reach the result the parties wish to gain. In fact, it is hardly possible for EU to invent sanctions that would severely damage Russian economy without equivalent economic damage to EU and vice versa – Russia and EU are too economically dependent on each other. The only result of the 'sanctions war' is that EU and Russia are now more isolated from each other. ■

Economic relations by its nature are beneficial for both sides, and the benefit is lost for the both if relations are suppressed.



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# Human capital in Nordic Countries and Estonia: PIAAC-based assessment

Expert article • 2168

Over recent decades, economic literature put a special emphasis on human capital as a core driver of economic prosperity and social well-being. High human capital is an essential component of countries' economic competitiveness in globalized world. Amount and quality of human capital determine economic potential and also play an important role in cross-country cooperation including also cooperation between the Baltic Sea Region countries. Therefore, it is extremely important that every country and region have good information on available human capital and possibilities of its development. This requires putting emphasis on assessment and comparative analysis of human capital.

With its roots in Adam Smith's theory (1776), the concept of human capital refers to knowledge, skills, competences and other attributes embodied in individuals that are relevant to economic activity. The theory of human capital aims to provide grounds for making the decision regarding an extent to which current resources should be invested in human capital. The criterion for such investment is the highest pay-off through improved productivity, employment and wages.

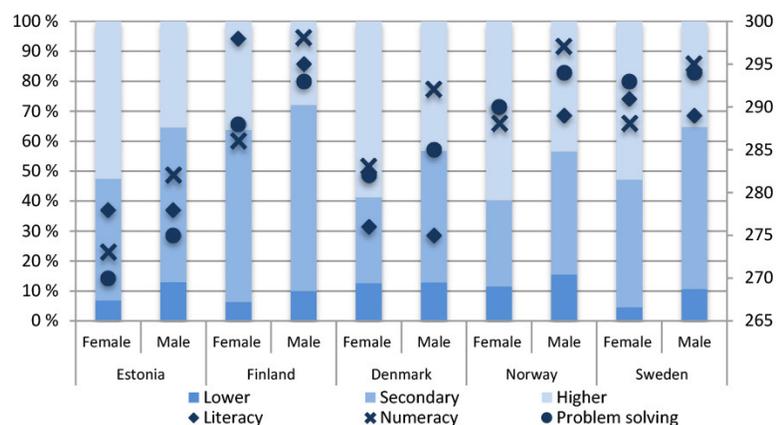
Thus, human capital is entirely embodied in personal abilities, competencies and skills, acquired and developed throughout a lifetime. Consequently, to precisely assess human capital, one needs to have an exact measure of individual knowledge and ability, applicable on the labour market. Lack of these data explains why most of the economic studies use former education solely as a proxy for human capital. Education by itself is an important, though not a sole channel of human capital formation. Abilities develop in family, workplace and through social acquaintances.

Therefore, our analysis comprises both formal education and actual measured abilities in three information-processing domains: literacy, numeracy and problem solving in technology rich environment. The data for our study comes from the Program for the International Assessment of Adult Competencies (PIAAC). The ultimate benefit of PIAAC data is availability of individual measures of cognitive skills in three aforementioned domains. The survey was conducted in years 2011-2012 in 24 European and non-European countries among individuals aged 16 to 65, and cognitive skills were assessed in 0-500 points scale. To evaluate the cross-country variation in human capital attainments, we compare Estonia to other Nordic countries, namely Finland, Denmark, Norway and Sweden. Due to numerous economical, political and cultural links Estonia has been previously analysed in the framework of Nordic region (Torben et al. 2015). Moreover, substantial differences in economic and social indicators in Estonia vs. the rest of the Nordic states make

comparative approach particularly appealing.

Figure 1 compares Estonian and Nordic countries with respect to two components of human capital: formal education and cognitive abilities of full time working people. The noteworthy fact is that men and women in all analysed countries possess average cognitive skills above 250 points. Thus, Estonia and Nordic countries performed relatively well in the international comparison. However, among five investigated countries, Estonian respondents, both men and women, scored the lowest points in numeracy and problem solving domains. Namely, average numeracy scores for Estonian males and females are 282 points and 273 points respectively with corresponding averages of 293 and 284 points across all analysed countries. Similarly, in problem solving males score 275, whereas females 270 points, being respectively 12 and 15 points less than average across all states.

Whereas, average formal educational attainments of males and females in Estonia are better than of Finnish men and women. Namely, 53% of Estonian full time working females and 35% of males hold university degree, relative to respective 36% and 28% among Finns. Remarkably, we found Finland to have the highest numeracy and problem solving measured for both men and women.



Educational profiles and average skills of full-time working males and females across Nordic countries and Estonia

The detected lack of correspondence between formal education and actual skills in case of Estonia supports an assumption that notable share of cognitive skills, as a part of human capital, forms beyond formal education. Estonian labour market may not put a sufficiently challenge and induce a development of their skills. While Estonian

youth show the best scores in PISA test among OECD countries<sup>1</sup>, older generation experiences a lack of skill development. The latter can be partly explained by the current role of Estonian economy in international division of work and orientation on the activities producing low GVA.

Another important aspect of human capital assessment is gender disparity in education and skills. Investments and human capital accumulation process may differ across men and women. Specialization and division of work within the family and job interruptions due to maternity and childcare leaves, as well as generally lower labour market commitment of women often result in staying partly or even fully outside a labour market. Eventually, women accumulate less human capital in the form of labour market experience, resulting in persistent gender variation in human capital profiles even despite their gradual convergence (Erosa et al. 2016).

Our findings affirmed that despite on average better educational profile, men out-perform women in numeracy and problem solving domains in Estonia. Similar pattern was documented for Denmark, Norway and Sweden, where men were found to more often reach high numeracy scores while holding relatively low formal education. Women in these countries are more often holding university degree, albeit having numeracy and problem solving abilities lower than males. This finding sheds more light on the ever-green gender wage gap issue (Blau 2016). It provides additional explanation to persistently higher earnings of males, as those can partly be attributed to men's higher cognitive abilities.

This, at the first sight, contradictory gap in female education and actual skills can be explained by the mechanisms of human capital accumulation. Important channels of ability development include practical training and on-job education, work experience, which may be gained by men to higher extent than by women, due to labour supply decisions and gender roles. Documented cross-Nordic differences in formal education and skill components of human capital reflect underlying disparities in returns to formal education across analysed countries. National labour markets may also facilitate on-job human capital accumulation differently through creating competitive and motivating work environment, as well as conducting targeted trainings.

To conclude, assessment and better understanding of gender variation in human capital should incorporate other channels than formal education and cognitive abilities. Non-cognitive skills and traits, such as self-confidence, risk aversion, attitude towards competition, personal motivation are important factors, both as components and drivers of human capital accumulation. These patterns require further in-depth investigation. ■

<sup>1</sup> See <https://www.oecd.org/pisa/PISA-2015-estonia.pdf>

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# Russia's technology push: What is it? Who believes what?

Expert article • 2169

**S**peaking at the January 2017 Gaidar Forum in Moscow, former finance minister Alexei Kudrin said: "We have to face the problem that Russia has fallen behind technologically in the world. That in my view, is the most serious challenge we face in the coming 10 to 15 years."

The Russian Government presently has a set of policies to directly propel Russia into the position of a world leader in high-technology industries. In my view, these policies are largely misguided and will fail.

The most recent of these is the National Technology Initiative (NTI) first mooted by President Putin in December, 2014. He said: "On the basis of long-term forecasting, it is necessary to understand what challenges Russia will face in 10-15 years, which innovative solutions will be required in order to ensure national security, quality of life, and development of the sectors of the new technological order."

Subsequently, a "long-term strategic plan" for the NTI, containing arrangements for "expert analysis, including the foresight method" was developed.

While at first glance the Government's policy approach might seem reasonable, it has four flaws that mean it is likely to be a policy failure.

Firstly, nothing is said about improving the use of existing technologies that could, in particular, allow Russia – like Australia – to turn the so-called "resources curse" into an advantage. As the World Bank recently noted, Russia's innovation "strategy focuses mainly on high-technology innovation with far less attention paid to catch-up innovation and building management skills in traditional industries, yet this is the building block on which more sophisticated innovation needs to be built." "Unlike Norway, Canada, and Australia, Russia does not appear to have developed a domestic extractives services and technology sector that would draw on the Russian innovation system."

Secondly, the high-technology industries envisaged are those that take advantage of future directions in digitalization to make Russia "one of the 'big three' major technological states by 2035". However, McKinsey researchers have noted that in regard to companies: "Given the speed with which new innovations, new markets, and new disruptions appear, creating a five- or ten-year plan is becoming an exercise in futility." The same can be said about planning for future Russian national technology.

Thirdly, the particular "foresight method" being used, called "Rapid Foresight", is a simplified version of the Delphi method for forecasting technologies that was developed in the 1950s. Despite the supposed credibility it gives to the choice of future technology projects to be supported with government funds, Rapid Foresight is really just an expensive version of "experts" sitting around a table.

Fourthly, NTI strategies include some dubious ideas about the world being increasingly divided into closed "economic-trade" blocs formed on the basis of a combination of economic and political issues,

each having the aim of developing and retaining production "value added chains" that are protected from outside competition. According to NTI documents, Russia needs to be part of – and lead – such a bloc. (This idea is the antithesis of the Chinese "One Belt, One Road".) The NTI strategy has always included an element of "import substitution". However, due to the influence of Crimea related economic sanctions, the importance of "import substitution" as part of the NTI seems to have grown.

Prime Minister Dmitry Medvedev, in an "original research article" paper published in December by the Kudrin edited "Russian Journal of Economics", wrote that Russian "structural reforms" require "rehabilitating the business climate and improving the quality of public administration". However, he also wrote that the "core of the structural reforms is import substitution". He goes on to claim that he means "smart" import substitution; not only are imports "squeezed out of the domestic market but also producers and products should be brought out that would be competitive in the global market". "Gearing industrial policy towards creating our own Russian (or, to be precise, Eurasian Economic Union) value chains should become a target for government incentives and support." Although Russia already bans certain imports, Medvedev's article is often confusing as he also talks about the improving the "investment climate" to promote "import substitution" and says that "import limitations often become export limitations" because "components are produced in different countries".

At the Gaidar Forum, Kudrin also said: "We will struggle with diminishing defence potential and threats to national sovereignty if we don't become a technological power. Even military experts say that technological challenges facing Russia are bigger than the geopolitical and military ones." "Our entire foreign policy should be subordinated to the task of technological development."

But what does this mean? More or less NTI and "import replacement"? For Putin it might mean more. It is less clear what Medvedev and Kudrin think. ■

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# Towards circular economy in Latvia

Expert article • 2170

**A**mbitious Circular Economy Package adopted by the European Commission requests active reaction not only from state institutions but also from companies and society members. Possibly because of the fact that Circular Economy Package emphasises recycling and clear targets for reduction of waste, it has misleadingly created an impression that a circular economy is related mainly to waste management. Therefore it is important to increase society's awareness that a circular economy is a much broader concept that includes a full lifecycle of products. According to Ellen McArthur's Foundation definition, a circular economy is one that is restorative and regenerative by design, and it aims to keep products, components and materials at their highest utility and value at all times. This broad concept includes using recycled materials, increasing longevity of products, industrial symbiosis, switching to bio based materials, as well as new consumption patterns, like sharing or collaborative economy and substituting products for services.

It is crucial to improve understanding that the circular economy has an important role in solving many current environmental problems, like climate change, resource depletion, increase of pollution, ecosystem degradation, biodiversity loss and others. It provides big opportunities for businesses to save costs and find new markets. It must be acknowledged that not only technical solutions but also social innovations and change of consumers' behaviour are completely necessary. Because of the rebound effect, it is impossible to solve the resource depletion problem only by improving technologies.

For the development of a circular economy in Latvia several prerequisites are necessary:

- assessment of the most prospective economy sectors for the circular economy, including bioeconomy and promotion of the possibilities to save materials and energy, and reduce the environmental impact;
- development of a national circular economy strategy;
- closer and more efficient collaboration between different ministries, municipalities and businesses; integrating circular economy aspects in the everyday decision making process;
- inclusion of the development of competencies necessary for the circular economy not only in studies of technical and natural science programmes, but also in business, economics and public administration study programmes and lifelong learning. Without knowledgeable and skilful managers and civil servants, development of the circular economy is encumbered;
- research in social and behavioural sciences regarding principles of the circular economy. This research should provide suggestions how to persuade people to share, to return products for reuse or recycling, to make responsible purchase decisions, use fiscal and non-fiscal incentives, predict unintended consequences of regulations, etc.;
- clarifying and adjustment of the existing legal framework regarding different sharing economy activities;
- creation of appealing narrative for society, development of easy understandable terminology in Latvian for many new circular economy aspects. We need common understanding to be able to speak about new production and consumption patterns.

There are several initiatives in Latvia which facilitate the circular economy, e.g. introduction of new study courses and circular economy topics in business education, new companies for peer-to-peer car lending and peer-to-peer money lending, developed sharing, lending and re-selling platforms, popular co-working places, organized social network and meetup groups. People, who are already interested in these new possibilities, can find ways to contribute and participate in collaborative economy. Much more should be done in order to inform and educate broader audience, also businesses and policymakers about benefits and peculiarities of the circular economy. Besides, the gap between knowing and doing should also be filled.

There is a good advantage for post-planned economy countries to develop sharing economy. Firstly, because we have historical experience in sharing a lot of things which were unavailable or deficit during the planned economy period; secondly, the average income level and the purchasing power are comparatively low, which motivates to share things to reduce costs. On the other hand, psychologically, people do not want to return to such consumption patterns because they want to use benefits provided by the free market and want to own things they were longing for. With the new generation born after regaining independence becoming purchase decision makers, this obstacle could diminish.

We have good examples from other countries, where we can find inspiration for the development of the circular economy, like activities of Ellen McArthur foundation, social enterprise Circle Economy, case study from Denmark, the circular economy strategy for Scotland and many others. Change agents could be universities, state institutions and municipalities which could contribute in promotion and facilitation of the circular economy development. ■



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# BALTIC RIM ECONOMIES

Pan-European Institute



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