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**SAARA-SOFIA  
SIRÉN**

Futures approach  
to saving the  
Baltic Sea



**EITVYDAS  
BAJARŪNAS**

Hybrid threats:  
Lithuania's  
response

**ARTO RÄTY**

The Baltic Rim  
countries can  
lead the change  
for a cleaner  
world



**MAXIMO Q. MEJIA JR.**

Developing a regulatory  
framework for autonomous  
shipping



# BALTIC RIM ECONOMIES

The Pan-European Institute publishes the Baltic Rim Economies (BRE) review which deals with the development of the Baltic Sea region. In the BRE review, public and corporate decision makers, representatives of Academia, as well as several other experts contribute to the discussion.

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## EXPERT ARTICLES

<b>ELSI KATAINEN</b>	<b>4</b>	<b>GALINA GRIBANOVA</b>	<b>22</b>	<b>ZAIGA KRIŠJĀNE</b>	<b>42</b>
The Baltic Sea Region - US relationship in the current trade turbulence		Russia-NATO confrontation on the Baltic Sea		Seeing potential of young return migrants to Latvia	
<b>SAARA-SOFIA SIRÉN</b>	<b>5</b>	<b>IVAN KURILLA</b>	<b>23</b>	<b>EVIIJA KLAVE</b>	<b>43</b>
Futures approach to saving the Baltic Sea		US – Russian relations as international manifestation of domestic culture wars		Third country nationals' integration in Latvia	
<b>JAAKKO OSSA</b>	<b>6</b>	<b>MARCIN KACZMARSKI</b>	<b>24</b>	<b>NICO GROENENDIJK</b>	<b>44</b>
Corporate income tax in Finland		Russia and China: fellow travellers		The Baltic States: Affluent societies?	
<b>EITVYDAS BAJARŪNAS</b>	<b>7</b>	<b>MARK D. STEINBERG</b>	<b>25</b>	<b>GEDIMINAS VITKUS</b>	<b>45</b>
Hybrid threats: Lithuania's response		The Russian revolution in prison: When history matters		The Euroscepticism in the Baltic States: Manifested and latent	
<b>CEES BANSEMA</b>	<b>8</b>	<b>OLAVI ARENS</b>	<b>27</b>	<b>KĀRLIS KRĒSLIŅŠ</b>	<b>47</b>
Dutch-Finnish economic relations		Brest-Litovsk in retrospect: A hundred year		Role of education in regional development: A case of Ventspils	
<b>IMANTS LIEĢIS</b>	<b>9</b>	<b>PAVEL TRUNIN</b>	<b>28</b>	<b>FRANKA MARIE HERFURTH</b>	<b>48</b>
Russia's impact on regional security		Russia's external debt		Cross-border vocational education and training	
<b>ALEKSANDR JEFIMOV</b>	<b>10</b>	<b>ALEXANDER BULATOV</b>	<b>29</b>	<b>SIGITAS BRAZINSKAS</b>	<b>49</b>
Narva is running for the title of European Capital of Culture in 2024!		Offshore orientation of Russian FDI		Digital industrial platforms as enablers of a closer Nordic integration	
<b>TURO MATTILA</b>	<b>11</b>	<b>MARIA ZOTOVA &amp; ALEXANDER SEBENTSOV</b>	<b>30</b>	<b>ALEKSANDR IZGORODIN</b>	<b>50</b>
Our cybersecurity requires European deterrence		New challenges to the cross-border cooperation in the Kaliningrad region		Lithuanian manufacturing: Rapid growth accompanied by challenges	
<b>MARIUS LAURINAVIČIUS</b>	<b>12</b>	<b>HELI SIMOLA</b>	<b>31</b>	<b>ALEXANDRA MIDDLETON &amp; ANDREY MINEEV</b>	<b>51</b>
Russian meddling in Western politics has been simplified		Finnish-Russian trade recovering gradually		What are the business opportunities and development challenges in the Arctic?	
<b>WOLFGANG SCHARECK</b>	<b>13</b>	<b>SVETLANA STEPANOVA</b>	<b>32</b>	<b>AKI PULLI</b>	<b>52</b>
On the way to becoming a beacon of excellence in the Baltic Sea Region		Cross-border tourist routes in the Finnish-Russian borderland		Ukraine's increasing presence in Baltic region	
<b>PIOTR STEPNOWSKI</b>	<b>14</b>	<b>ADAM A. AMBROZIAK</b>	<b>33</b>	<b>TIINA RITVALA</b>	<b>53</b>
University of Gdansk in Baltic Sea region		Russia's embargo on the Polish apple exports		Grand challenges and the small wins strategy	
<b>ARTO RÄTY</b>	<b>15</b>	<b>MERIT TATAR</b>	<b>34</b>	<b>ALEKSANDRA WĄSOWSKA</b>	<b>54</b>
The Baltic Rim countries can lead the change for a cleaner world		Developing smart and sustainable urban transport systems		Political and social strategies of multinationals in Sub-Saharan Africa: A focus on Polish firms	
<b>KEITH MARTIN</b>	<b>17</b>	<b>MAXIMO Q. MEJIA JR.</b>	<b>36</b>	<b>MATTI POKKALA</b>	<b>55</b>
Nord Stream 2: A European project in the Baltic Region		Developing a regulatory framework for autonomous shipping		Cuba attracts more than ever – Bokira's view	
<b>TADAS JAKŠTAS</b>	<b>18</b>	<b>MILLA HARJU</b>	<b>37</b>	<b>KARI LIUHTO</b>	<b>56</b>
Maritime threats to energy security in the Baltic Sea region		Global challenges call for local response through common goals		The future of Cuba: Reform or revolution	
<b>MIRIAM HOLSTEIN</b>	<b>20</b>	<b>LEONARD ROZENBERG &amp; DARIUSZ ZARZECKI</b>	<b>38</b>		
Open innovation is the key to success also in the Nordic region		Shipbuilding – reality and challenges for Poland			
<b>EVGENY LEBEDEV</b>	<b>21</b>	<b>TOMASZ ABRAMOWSKI</b>	<b>41</b>		
Belarus-Finland investment cooperation		Deep sea mining – raw materials new perspective			

ELSI KATAINEN

# The Baltic Sea Region - US relationship in the current trade turbulence

Expert article • 2394

Talking about global trade these days is a tricky matter, especially global trade relations with US is a challenging topic. As EU Member states, all the Baltic Sea countries are under the EU external trade policy. For this very reason, it is hard to examine these countries as separate from the rest of the Union. What makes these countries even more relying on the common trade policy set by the EU, is the fact that their economic stability relies heavily on external trade.

During the past couple of years, namely after the election of the current president of the United States, global trade has been under pressure. Three years back, the future still seemed bright: EU was part of various ambitious plurilateral negotiations such as the Environmental Goods Agreement (EGA) and the Trade in Service Agreement TISA. EU was even negotiating a bilateral trade agreement with the US. No doubt, closing these agreements would have been a great victory for EU, EGA especially for the Nordic member states. Times have changed since. Consequences of Brexit and number of protectionist trade measures have dominated recent debate at the International Trade Committee of the European Parliament.

Most of the Baltic Sea countries are, just like Finland, depending on the global trade and global value chains. These countries are not self-sufficient in raw materials or in energy, and their economic growth relies mainly on goods and services sold at external markets. These factors underline the importance of the current inflammatory state of global trade and trade relations with US. Market changes of the near future seem challenging to predict and our trade relation with the US remains uncertain. The current US administration has proven to be unpredictable trading partner and this can make global trade, especially investments related to US trade, unattractive for European companies.

EU-US block accounts for more than fourth of the global GDP per year and US remains to be one of EU's biggest trading partners. This relationship has been shadowed by the ongoing discussions of new tariffs that could harm the trade between the continents. After the steel tariff dispute spurted last spring, an interesting fact was brought up, a point which describes well the current irrationality of Trump's trade policy: the proposed tariffs on European manufactured steel would not even cover the asymmetric of the trade statistic EU and US share on the bilateral trade.

Global trade and trade relations are like domino blocks: when one falls, others will follow. The instability of the current EU and US trade relations is only a side effect of a bigger picture. The main enemy for Trump in his pre-trade war is China. However, every action US is now taking to block China from global markets is bringing the giant Eastern

economy closer to EU. Simultaneously, US is creating distance between its own trading partners. In addition to China, the US-Russia trade relationship can, when taking unexpected turns, reflect strongly on EU, especially when it comes to EU's energy policy and supply. Every increased tariff or import quota US launches makes its trade partners, EU among the quickest, to look for other reliable partners to import raw materials from and markets to export our products to. Protectionism harms all.

The harm US creates with its current trade policy has unlimited number of negative consequences. For Baltic Sea region, and for the whole EU, one of them is the risk of jeopardizing the functionality of the World Trade Organisation (WTO). In today's global trade, it is merely impossible to speak about a functioning and fair, rule-based trading system without WTO. The actions US serving president has taken to weaken the global trading institution is astonishing. The fact, that US is no longer willing to trade according to jointly set rules and norms is not beneficial to anyone, especially to US itself, in the long run.

Although Europe now must look for alternative trading partners by signing ambitious agreements, such as the one with Japan, it is equally of important for EU to continue dialogue with US. We must keep engaging good trade relations with countries and markets, who share our values and beliefs. US is a one of our main trade partners and this relation is one to keep. With its unanimous and consensus-seeking trade strategy, EU has proven to be the world's strongest and stable trade front. This line needs to continue in the future. Constructive negotiations, yet firm stand underlining the importance of global rule-based trade, is the only way to navigate in the storm. It is also crucial that we have like-minded trading partners who will proceed the same way. EU should not turn its back to US but work actively to stabilise the global market and guarantee that our companies have partners to trade also in the future. In this light, Baltic Sea region can act as a forerunner in EU trade policy. ■

The instability of the current EU and US trade relations is only a side effect of a bigger picture.



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SAARA-SOFIA SIRÉN

# Futures approach to saving the Baltic Sea

Expert article • 2395

**B**asic idea in Futures studies is that the future cannot be predicted – but alternative futures can be forecasted. Take for example eutrophication of the Baltic Sea. We would need to set a goal, a preferable future scenario of the ecological status of the sea, and then accordingly take a path of measures which lead us towards this goal.

To have this kind of foresight, we would need to scan the environment and form an understanding of the current situation. Thus, to understand the status of the Baltic Sea from a wider perspective than just the numbers of algae growth, we would need a comprehensive view of the situation.

Eutrophication is not only an environmental question, but an economic and social question too. Furthermore, it has political and technological aspects. These five qualitative variables could form a simple PESTE analysis (political, economic, social, technological, environmental), a tool that identifies the key external factors affecting to eutrophication of the Baltic Sea. A simplified analysis starts with what we already know.

## Political:

Several international agreements, programs and commitments have been conducted throughout the years regarding the wellbeing of the Baltic Sea. On EU level, one of the key documents is Marine strategy framework directive. Another one is Water framework directive. One important document is the European Union Strategy for the Baltic Sea Region (EUSBSR). Saving the Baltic Sea is one of the three key aims of the strategy. All coastal states and the EU are committed to the HELCOM "Baltic Sea Action Plan" -programme. Eutrophication has also been one of the main themes within Nordic co-operation. Wellbeing of the Baltic Sea is a topic also in the Northern Dimension Environmental Partnership (NDEP). All these documents form a basis for the political discussion regarding eutrophication of the Baltic Sea.

## Economic:

The worrying situation of the Baltic Sea can be seen as a market failure. The bad condition causes costs. It has been calculated that decreasing eutrophication would bring economic benefits for the region worth of 3,6 billion euros. The benefits are greatly bigger than the costs of reducing nutrient load. Water pollution can in fact be regarded as an external cost, which requires action from the governments concerned. On the other hand, Circular economy has hundreds of billions of market potential. Eutrophication of the Baltic Sea therefore has economic affects that go both ways: bad condition costs more than it would cost to fix the problem, plus the solutions enable significant possibilities for growth.

## Social:

The condition of the Baltic Sea affects not only our natural heritage, but the wellbeing, livelihood and health of the 85 million people living around the sea. Unfortunately, people do not always seem to understand the role of human actions in both causing and solving the situation. According to a survey by Swedish Environmental Protection Agency (2010), people living around the Baltic Sea have

very varying attitudes regarding the status of the sea. The numbers differ from country to country, but in some countries less than half of people state that they are worried about the Baltic Sea environment. Eutrophication of the Baltic Sea affects to the lives of all people living in the region, however, most people do not think that their own actions play a role in improving the status of the sea.

## Technological:

Circular economy could be the solution to decrease the nutrient inflow that causes eutrophication. A key idea is to recycle nutrients from agriculture so that instead of the nutrients causing environmental load, they would be re-used.

Multiple innovations based on the idea of re-using nutrients already exist. There are projects bringing together research, decision-making and private funding with the aim of supporting eco-technologies with circular economy approach in the Baltic Sea region. To reduce eutrophication of the Baltic Sea, we need to take advantage of short-term solutions specifically targeted to most vulnerable zones. Nevertheless, more important than temporary measures are long-term solutions that aim at reducing nutrient input already in the first place.

## Environmental:

Eutrophication is a major problem in the Baltic Sea and repairing the damage is a complex and time-consuming task. The results may become visible only after a long period of time. Unfortunately, climate change will only worsen the problems caused and threats posed by eutrophication. Surface waters will become warmer as average temperatures rise. Another predicted consequence is an even higher amount of rainfall. Global climate change will significantly amplify the effects of nutrient load. Eutrophication is still affecting the Baltic Sea, despite the fall in the amount of phosphorus and nitrogen. The challenge is not getting any easier.

So why is it that we fail repeatedly to meet the standards that we have set together? I think that one of the main reasons is the fact that the political perspective is too short. To understand the future of the Baltic Sea, a wider perspective would be needed. Political decision-making could benefit from future oriented research and long-perspective visions. Furthermore, we just need more courage to bring the questions of future generations to the center of today's political agenda. ■



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JAAKKO OSSA

# Corporate income tax in Finland

Expert article • 2396

**1 General presentation of Corporate Income Tax in Finland**  
A corporate entity is separately liable to pay tax (=opaque) and it pays tax according to the corpo-rate income tax base which is 20,0 per cent in 2018. The shareholders of a corporate entity are only liable to pay tax for the income that is distributed to them by the company, for example, as divi-dend.

A partnership is not separately liable to pay tax (=transparent). Taxable income for the fiscal year is verified for a partnership, but the taxable income is for tax purposes distributed to the shareholders according to the shares they have in the income of the partnership. Foreign entities cannot opt to be treated as either transparent or opaque. If a foreign entity is comparable with a corporate entity registered in Finland (for example, Aktiengesellschaft in Germany or aktiebolag in Sweden), it shall be directly considered a corporate entity by virtue of the law in Finland, and therefore the entity cannot choose its taxation status.

The corporate income tax base is dependent on international tax competition, and in Finland the Government has undertaken to follow the development in key comparison countries. If the corpo-rate income tax base is generally lowered in the comparison countries, the corporate income tax base may also be lowered in order to maintain the position in the tax competition. Corporate in-come tax is extremely exposed to economic fluctuation, and hence the decisions concerning the corporate income tax base also include other affecting factors in addition to international tax com-petition.

## 2. Historical evolution of Corporate Income Tax

The taxation model in which corporate entities are separately liable to pay tax has been the preva-lent model in Finland for decades. Taxable income is confirmed for corporate entities by virtue of the *Business Income Tax Law* (BITL). The regulations concerning the taxation of the profit distribut-ed by a corporate entity and other distribution of assets are found in *Income Tax Law* (ITL). The regulations concerning the taxation of dividend income in particular have changed a number of times. From the year 2005 on, the distribution of profit has been taxed according to modified dou-ble taxation, in which the company is taxed for its taxable profit (20,0 %) and shareholders are taxed for the dividend paid by the company.

Dividend received by a corporate entity from another corporate entity is, however, generally tax free income. The stipulations of the Council Directive on the common system of taxation applicable in the case of parent companies and subsidiaries (90/435/EEC, 2011/96/EU) have been taken into account in the taxation of dividend income. There are many different alternatives for the taxation of dividend income, depending on what kind of a company pays the dividend and who receives the dividend.

## 3. Cross-border situations

In Finland a corporation can be generally liable to pay taxes or it may have limited tax liability. In Fin-land a corporation generally liable to pay taxes is paying tax to Finland for their global income, i.e. the income received from Finland and elsewhere. A corporation with limited tax liability only pays taxes to Finland for the income received in Finland.

A domestic corporation is generally liable to pay taxes in Finland. The corporation is domestic if it has been established and registered under the Finnish legislation. The nationality or place of resi-dence of the owners or management of a corporation registered in Finland have no significance. Similarly, a European company (SE) or a European Co-operative Society (SCE) registered in Finland is treated as a domestic corporation in taxation (*Section 8 a of ITL*).

A foreign corporation has limited tax liability and pays tax to Finland only for the income received from Finland. Having the company management in Finland does not alone make a foreign company a domestic corporation i.e. generally liable to pay taxes to Finland. If a foreign corporation has per-manent establishment for its operations in Finland, the corporation is liable to pay tax on the basis of its income for all the income classified to belong to this permanent place of business.

If another country considers that due to the management of a company registered in Finland being located in that country the corporation is generally liable to pay tax in that country, there will be a risk of double taxation: the corporation is taxed for its global income both in Finland and in the oth-er country (dual residence). In this case the conflict shall be settled by applying the article on con-flict resolution in the tax treaty between Finland and the other country (cf. OECD model tax treaty article 4.3).

In tax treaties between Finland and another contracting country for the prevention of double taxa-tion, it has been agreed on the division of the tax basis between Finland and the other contracting state. The articles of the tax treaty are applied prior to ITL (priority). The tax treaties entered into by Finland follow rather closely the structure of the OECD model tax treaty.

The internal law of Finland contains the definition of permanent establishment. The tax treaties made by Finland also define the permanent establishment, and the tax treaty is applied prior to ITL (priority). According to the tax treaties corporations are primarily taxed for the business profits re-ceived by them only in the country of residence of the corporation. Finland as a contracting state can impose tax on the business profits of a foreign corporation only if the company runs its opera-tions in permanent establishment in Finland (see OECD model treaty articles 3.1c and 7). ■



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# Hybrid threats: Lithuania's response

Expert article • 2397

Let me start from the general picture. It looks very obviously that in parallel to its aggressive military posture, over the last years Russia advanced in the field of hybrid warfare. Most visible examples: continuous aggression in Eastern Ukraine, military intrusion in to Syria, meddling into national elections and referendums, poisoning of Skripal family, supporting radical political parties, confusing decision-making. Russia's strategic goals are to question post-WWII system, to change the global power balance, to divide Trans-Atlantic community, to dominate within its perceived zone of interests, including the Baltic Sea Region, to bring ambiguity, and to work on our weaknesses, especially using hybrid tactics.

Countries, including Lithuania, or their groups are facing an important dilemma - how to deal with such types of threats that are below traditional war?

In case of the Baltic States, Russia has long been using political, economic, energy resources, propaganda, cyber, informational and other coercive, overt and covert means for years.

In case of Lithuania, Russian intelligence and security services conducted influence operations in support of Russia's aggressive policy against Lithuania and were particularly interested in the upcoming Lithuanian presidential elections in 2019. Most identified hostile cyber activities in Lithuania were related to Russia. Russia's hostile hybrid strategies against NATO's enhanced Forward Presence were also noted. Russia conducted aggressive information, historical and ideological policy against Lithuanian (eg. to demonstrate perceived Lithuanian society's disapproval of domestic and foreign policy, to fuel anti-Western sentiment). Russia continued its attempts to dominate the energy market of the Baltic region and obstruct its integration into the Western Europe energy system. Belarus together with the Russian corporation Rosatom accelerated the construction of the Ostravets Nuclear Power Plant, failing to comply with the international nuclear security requirements. In a wider scale, Russia also skilfully employed conspiracy theories, alternative truths, lobbying, discredited states in the international arena, harassed those who criticize the Kremlin, and promoted its narratives. List of Russia's hybrid actions could be continued.

So, how to counter hybrid threats? What are Lithuania's responses to overcome them? Key national response elements set out below for tackling hybrid threats:

- Have a strong political mandate and a comprehensive security concept. The Lithuanian National Security Strategy (newest version, updated in 2017) uses comprehensive approach to security.
- Develop a system for understanding hybrid threats. Since 2014, the Lithuanian authorities - the MoD, army, intelligence, police, and border guard services (listing only a few) have taken specific actions against the hybrid threats.
- Have good level of coordination between the various institutions at the Government level and have a crisis management mechanism,

to prepare and work the procedures of various institutions.

- Have a common understanding of the situation, a common threat and risk assessment, and planning and training processes by key stakeholders. The key decision was to increase the defense budget so that it would even exceed the 2 per cent of GDP. The conscription system was restored and the rapid reaction forces were set up. Regular exercises with the hybrid scenario.
- Set up cyber defence system focusing on the protection of critical information infrastructure, the public sector, increased resilience and response capability.
- Implement counter disinformation steps, ie strengthening strategic communication; raising public awareness of information wars and propaganda; suspension of the propaganda of war and hatred. Not only the education of officials, politicians, the media and society has become an important issue in the fight against information threats, but also active communication in identifying lies, deconstructing it, developing the message and narratives of Lithuania itself.
- Set up national integration and development of regional policy.
- Make a breakthrough in ensuring energy independence.
- Amend legal acts to respond to hybrid warfare.

Besides, fighting against hybrid threats relies not only on national but also on collective – NATO and the EU – efforts. International cooperation, particularly through the NATO and EU, but also using regional and multilateral initiatives such as Nordic-Baltic cooperation, European Centre of Excellence for Countering Hybrid Threats, can offer much on the political, economic and military fields. Besides, this helps “covers” some missing national capabilities or render support in developing these capabilities in the areas in which they are not sufficiently developed. International cooperation enables to unite separate, scattered national resources in solving issues of a broader international agenda. ■



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CEES BANSEMA

# Dutch-Finnish economic relations

Expert article • 2398

In January 1918, less than six weeks after its proclamation of independence, Finland was recognized as a sovereign state by the Netherlands. Thus, the year 2018 has been marked by both our countries to celebrate the centennial of uninterrupted friendship and political relations.

Of course, economic and commercial relations between our two countries date from way before Finland's independence. In the second half of the 16<sup>th</sup> century Dutch ships started to trade with Helsinki merchants. Salt was brought from the Netherlands and was traded for tar, an important commodity to preserve the lifespan of ships. In the 17<sup>th</sup> and 18<sup>th</sup> centuries, Finnish timber was used by the Dutch East and West Indies companies for building a massive amount of merchant ships. Over the years trade became also more diverse; Dutch banks started to finance the Finnish entrepreneurs (like the owners of sawmills) and Dutch businessmen established themselves into Finland. One example is a Thomas Matthijsen, who moved in 1730 from the Netherlands to the town of Hamina. In the 19<sup>th</sup> century, when Finland started to industrialize (and to urbanize), study trips by industrialists and local governments were made, mostly to Sweden and Germany, but also to the Netherlands, in order to get ideas for both industrial and urban development in Finland. One striking example was the visit of the Helsinki city officials at the turn of the century to the Netherlands to study our urban water supply system, including chemical purification of waste water; a revolutionary process in those pre-independence days.

Though interesting as it is, this contribution will not focus on the economic history between our countries. Rather I would like to push the 'fast forward button' to where we stand now: two smaller, but very prosperous nations who are both in the core of the European Union. The core, as Finland and the Netherlands established the Eurozone and had its currency from day one onwards. This distinguishes Finland from its Nordic neighbours. Also the core as neither of our two countries has asked for any opt outs in the European integration. In short; we take actively part in all areas of EU cooperation, without reservations.

Last year (2017) bilateral trade stood at over 8.8 billion Euros, with a slight advantage of the Netherlands over Finland (Dutch exports being 4.5 billion Euros, Finnish exports being 4.1 billion Euros, source: Dutch statistical office CBS). Looking closer at this figure it is quite spectacular, given the aggregate population of our two countries. Actually, it makes the Netherlands the third export destination for Finnish business (after Germany and Sweden) and the fifth source country for Finnish imports (after Germany, Russian Federation, Sweden and China). Finnish exports to the Netherlands are mainly found in SITC-category 6 'other manufactured goods', whilst Netherlands exports to Finland are to be found in SITC-category 7 'machinery and transport equipment'. It is to be expected from two highly developed nations that the bulk of our trade consists of goods with a local added value, rather than raw materials (although we do trade in that as well). Interestingly enough, the products that one (stereo) typically associates with our two countries have a small weight in our export baskets; Dutch dairy amounted to 25 million euros (= 0.5% of our exports to Finland) and Finnish pulp and paper to 138 million euros (=3.3% of Finnish exports to the Netherlands).

Given these high trade figures one would expect large economic sections in the Dutch embassy in Helsinki and the Finnish embassy in The Hague. Neither is the fact. There are several good reasons

for a small role of government involvement in our trade. In the first place our countries are glued together into the European Union's Single Market, with its four freedoms of persons, goods, services and capital. This makes transnational trade much less cumbersome than trade with third countries. Moreover, within this Single Market, the Netherlands and Finland are both in the top-position of different charts such as 'ease of doing business' (World Bank) and (lack of) 'corruption perception index' (Transparency International). In practice, this means that a Dutch or Finnish company seldom needs to seek help from its government (eg through its Embassy) when it is entangled in a business dispute. Also, it is rarely necessary for us to 'hand hold' a Dutch company, which wants to have access to a Finnish customer. In general Dutch and Finnish companies are more than willing to meet foreign prospective business contacts, provided they have a good 'pitch' and, of course, a product or a service with the right price/quality combination. The fact that both Dutch and Finnish business has a good command of English is of course helpful!

Nevertheless, the Netherlands Embassy in Helsinki is very active to help promote business. We help individual Dutch companies (with a focus on the Small and Medium-sized Enterprise segment) with requests on market opportunities. A concrete product is the 'business partner scan', tailor made for the applicant. Also, we promote and support incoming sectoral missions to Finland, which may be accompanied with a visit to a trade fair (including the setting up of a Dutch pavilion).

Based on the potential in Finland and the expertise of Dutch exporting companies our focus areas are the theme 'smart and sustainable cities' (think of waste collection, sustainable building, smart traffic solutions), healthcare (both medical equipment as hospital construction) and –more cross cutting the different themes– start-ups. The annual tech-event Slush in Helsinki is considered as one of the leading events of its kind worldwide and attracts many Dutch start-ups. Our embassy has a prominent spot in this event and organizes thematic side events. We are not confined to Finland's capital. We have also been active on similar start-up events in Oulu (Polar Bear Pitching) and Turku (Shift).

A recent addition to our tasks has been a project on Circular Economy. Both the Netherlands and Finland belong to the front-runners in this field. We can learn a lot from each other and establish contacts between business communities, innovation-labs in universities and between local governments.

I like to invite readers of this article with any more detailed questions or comments to contact the Embassy via the e-mail-address [HEL-EA@minbuza.nl](mailto:HEL-EA@minbuza.nl) ■



CEES BANSEMA

Ambassador of the Netherlands to Finland



IMANTS LIEĢIS

# Russia's impact on regional security

Expert article • 2399

Security in the Baltic Sea Region and beyond changed radically in 2014. One of the regional powers, Russia, illegally annexed Ukraine's territory in Crimea. Subsequent military action in Eastern Ukraine has resulted in an ongoing war in the neighbourhood. The shock waves caused by Russia using military means for political ends continue to be felt today. There is no immediate solution to the conflict in sight. The first "alarm bell" concerning Russia's role as a spoiler of post-Cold War amiability of course rang loud and clear in 2008 with the military intervention in Georgia.

As at autumn 2018, what are the repercussions caused by Russia's aggression?

Euro-Atlantic unity in response to these events has been resilient. Sanctions were imposed at an early stage with the EU closely coordinating its approach with the USA. NATO has pursued a consistent approach of increasing defence and deterrence in its Eastern flank (Poland and the Baltic countries) whilst remaining open to dialogue. USA, Canadian, UK, German, French and other troops have been deployed to this region to reinforce the solidarity element of NATO's collective defence whereby an attack on any NATO member would be seen as an attack on the Alliance as a whole. These measures have been commensurate with the increased threat perception. Russia's unexpected military engagement in Syria and its use of a military-grade nerve agent on the territory of the United Kingdom earlier this year have hardened the approach of the Euro-Atlantic community. An ongoing display of firmness in this regard is imperative pending changes in Russia's behaviour.

Dialogue at various levels has recently been highlighted. Helsinki hosted the Trump-Putin meeting in July, just days after the NATO Summit in Brussels. As at mid-September, President Putin had met twice this year with both his German and French counterparts. Merkel's and Macron's engagement with Putin remain an integral part of the "Normandy Format" which seeks, together with Ukraine, a solution to Russia's occupation of Crimea and ongoing military action in Eastern Ukraine. Currently, the prospects of arriving at a solution seem dim.

A heightened awareness of the threat from Russia following its attacks on Ukraine has evolved in two crucial Baltic Sea countries that remain outside NATO – Sweden and Finland. Both have attended NATO summits in recent years and increased their cooperation with the Alliance. Finland's President Niinisto was reported to have said in August 2018 that Finland's NATO membership is a possibility. Sweden has reintroduced military conscription and restored its military garrison on the island of Gotland, its most eastern outpost in the Baltic Sea.

These reactions have been in response to Russia's activities, both outside the region, but also within the region itself. The last few years have witnessed large Russian military exercises by NATO

Eastern flank borders as well as a big increase in airspace violations and military aircraft approaching borders without transponders being turned on. Nuclear sabre-rattling has been demonstrated by Russia's leadership. In 2015, Russia's Ambassador to Denmark even threatened aiming Russian nuclear missiles at Danish navy ships if Denmark joined NATO's missile defence system. There have been reports this year that Russia has upgraded its nuclear storage facility in the Kaliningrad enclave on the Baltic Sea. This could allow the permanent presence of Russian Iskander – M missiles, capable of carrying nuclear warheads.

Nevertheless, the possibility of Russia militarily attacking a NATO country in the region is perceived as being small.

Russia involvement in hybrid threats has also impacted the region in recent years. Each Baltic country capital hosts a NATO Centre of Excellence dealing with these threats. Estonia led the way after it was hit by cyber-attacks in 2008 by establishing a Cyber Security Centre of Excellence. Lithuania holds the niche in energy security threats. Latvia has a centre on Strategic Communication. These are all centres linked to NATO. Last year Helsinki established a similar Centre - the European Centre of Excellence for Countering Hybrid Threats - the first of its kind to be set up within the EU framework. These four centres reflect the contemporary threats posed to regional security by various actors. The research and knowledge provided by these centres make an invaluable contribution to global security challenges extending far beyond the Baltic Sea region.

Other regional security questions for residents of the Baltic Sea region are being tackled by Latvia's current Presidency of the Council of the Baltic Sea States (CBSS). Priorities include: civil emergencies or catastrophes; the fight against human trafficking and; the challenges posed by organised crime. These issues allow for cooperation amongst all CBSS countries irrespective of security measures taken following the events of 2014. ■



IMANTS LIEĢIS

Latvia's Ambassador to France,  
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ALEKSANDR JEFIMOV

# Narva is running for the title of European Capital of Culture in 2024!

Expert article • 2400

Starting 1985, the title of the European Capital of Culture (ECoC for short) has been annually awarded to two cities within the European Union, with a couple exceptions. It is one of Europe's most famous and effective cultural initiatives, which provides to the title-bearer city intense international attention throughout the title year, constituting for most participating cities the largest cultural event in their history. Although technically a "cultural" project, for dozens of cities around Europe ECoC has served as a tool to reestablish themselves, bring to fruition long-awaited plans and make both a cultural and an economic leap forward.

The capital of Estonia, Tallinn, was the first Estonian city to bear the title in 2011, but in 2024, the European Capital of Culture will once again reach Estonia. And to everyone's surprise, on January 23<sup>rd</sup> this year, the Eastern-most city of Estonia and one of Europe's largest border towns, Narva, has decided to run for the title.

The official launch ceremony was held in Narva's historic City Hall and was attended by ambassadors of Finland, Sweden, Germany, Norway, Denmark and Austria, members of Narva City Council, representatives of cultural initiatives and entrepreneurs, and even the President of Estonia, Kersti Kaljulaid, herself. The distinguished guests were singing praise to Narva's decision, predicting bright times ahead for Estonia's border town.

## So what is the big deal?

Narva is a complicated city, simultaneously dividing and uniting two civilizations: the European North and the Slavonic East. It was an important trade port and an aspiring second capital of the Swedish Empire during the XVI-XVII centuries, as well as an important industrial hub during the Soviet times. However, given its traumatic history, a pattern of post-industrial decline and 96% of its 58,000 inhabitants (down from 82,000 back in 1992) speaking Russian as their mother tongue, the city has been struggling to find new meaning ever since Estonia regained its independence in 1991. Never a darling of the media, the city became especially notorious after the annexation of the Crimea in 2014, when noticing its geopolitical location, demographical buildup and structural problems, the foreign press flocked to Narva, asking "Is Narva next?"

Having grown weary of assuring its loyalty to Estonia and Europe, the city recently decided to turn this perception around with a confident reply "Narva is next!" reframing itself not as a fragile geopolitical time-bomb, but as Estonia's next big success story, a creative hotspot, making the most of the advantages of being a border city between the tectonic plates of Russian and European cultures.

Bidding for the title of the European Capital of Culture in 2024 will create a time window of valuable 6 years to develop a clear vision and a strategy to reinvent the border town, eventually encouraging the local community to make a leap from the industrial era to the post-industrial one. The city believes that culture, creativity, innovation and entrepreneurial thinking could help it turn the next page. Given its unique history, post-soviet quirkiness, difficult geopolitical location and plenty of space for radical improvement, Narva might be one of the most important ECoCs in the history of the project and an extremely timely one as well. ■



## ALEKSANDR JEFIMOV

Chairman of Narva City Council  
during April 2011- July 2018  
Estonia

Follow Narva on its path towards becoming the European Capital of Culture in 2024:

Email: [narva2024@narva.ee](mailto:narva2024@narva.ee)

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#Narvaisnext

#Narva2024

TURO MATTILA

# Our cybersecurity requires European deterrence

Expert article • 2401

European Security order is challenged in ways that many in the West thought belonged to a bygone era of the Cold War. Especially after the illegal annexation of Crimea by Russia in 2014, terms such as reflexive control, subversion and active measures have re-entered the vocabulary to describe unconventional security threats that we need to tackle. These malicious efforts to divide our societies and weaken us are called hybrid threats due to their multidimensional nature.

Increasing reliance of modern societies on Information and communication technology (ICT) means that hybrid operations that in the past took place in physical space now often take advantage of cyberspace. Disinformation campaigns, for example, use social media and the Internet as platforms, whereas cyberattacks aim at disrupting or destroying the target's ICT infrastructure. Due to the interconnectedness of these networks, cyberattacks often infect IT systems well beyond the original target and cause damage to individuals, companies and governments alike. This has been manifested for example by the NotPetya ransomware attack in the spring of 2017, damages of which have been estimated to run up to billions of US Dollars in over 65 countries. According to several Western governments, NotPetya was an operation of the Russian military's foreign intelligence service GRU. Several other countries and non-state actors have also been accused of carrying out hostile cyber activities in recent years. Cyberattacks are often part of a broader campaign that uses several hybrid methods in a coordinated manner.

Our everyday life, business and critical government functions rely on digital infrastructure often owned or operated by private companies. This underlines the need for a whole-of-society approach to building cyber security.

Protecting our societies against cyberattacks – and hybrid threats in general – consists of two parts: Resilience, which is the ability to recognize, repel, withstand and recover from hostile activities, and deterrence, which is the ability to discourage a hostile act through the threat of consequences for the aggressor.

Building resilience starts with all actors taking their own IT security seriously. Best expertise for developing new solutions to this end lies in the private sector. States, however, bear the responsibility for building a credible deterrence against cyberattacks. This responsibility cannot be outsourced to the private sector and companies cannot freely retaliate when they are attacked. Only governments have the executive power and legal authority to carry out countermeasures. Governments also bear the responsibility for making the right attribution, meaning evidence-based identification of the aggressor.

Cyberattacks are becoming more frequent and reckless because the cost-benefit analysis is favorable from the perpetrator's point of view: Hostile cyber activities have often gone unpunished.

This needs to change. Attacks in cyberspace can have disastrous effects for the population even without the use of conventional military force.

The European Union together with a broad coalition of like-minded countries works for universal recognition of the applicability of existing international law in cyberspace – including the UN Charter and its right of self-defense. We want to secure a free and functioning Internet and call for responsible state behavior.

In addition to strengthening rules-based international order, the EU is turning itself into a security actor that is able to protect European citizens and interests. Deepening EU defense cooperation encompasses the development of cyber capabilities. The EU is also an important partner for NATO in countering hybrid threats because of its diplomatic, financial and legal instruments. At the time of writing, 18 EU or NATO members have already joined the European Centre of Excellence for Countering Hybrid Threats in Helsinki.

EU member states approved in 2017 a cyber diplomacy toolbox that defines several ways to react jointly to cyberattacks. Possible joint action can range from 'naming and shaming' of the aggressor to imposing restrictive measures. Having a credible ability to make the aggressor pay through economic sanctions, travel bans and other legal means is crucial for building deterrence in cyberspace. Imposing sanctions requires a unanimous decision by all member states in the EU Council. This underlines the need for shared situational awareness and deeper cooperation particularly in intelligence and law-enforcement.

Since hybrid campaigns aim at increasing divisions within the EU, ability to name the perpetrator and decide on an appropriate response together would also send an important political message.

Cyberattacks are likely to increase unless they become unsuccessful due to the target's increased ability to protect itself, if consequences of an attack outweigh the benefits for the aggressor, or if the political aims of the aggressor change. By strengthening our resilience and deterrence, we will raise the threshold for anyone to engage in hostile activities against us. ■

The views and opinions expressed in this article are those of the author and do not necessarily reflect the official positions of the Government of Finland.



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MARIUS LAURINAVIČIUS

# Russian meddling in Western politics has been simplified

Expert article • 2402

**R**ussian election meddling has become an issue which is almost daily discussed across the Western world. However, it seems that the phenomenon we face is frequently simplified and reduced to cyber-attacks and disinformation campaigns. In other words, the information warfare element of the overall meddling mosaic, and, in particular, the role of the internet for spreading the Kremlin's influence, is mostly in focus. Meanwhile, malign Russian activities are much more comprehensive and utilize much more tools, while the whole process is far more multi-level and diversified than mere tactics of information warfare.

Moreover, viewing Russia's election meddling as a self-sufficient phenomenon in isolation from the Kremlin's long-term and comprehensive malign activities, is very likely to lead to the wrong conclusions about the meddling itself. For Putin's regime, meddling in the elections is only a part of a bigger campaign in the Kremlin's war against the West, carried out non-stop for a long time and using a variety of methods in its malign activities.

The Kremlin's support to its favorable groups is hardly limited to a particular election campaign. On the contrary, if support is successful in the long run and internal issues of the West are properly exploited, direct election meddling can become redundant or limited.

On the other hand, the process of meddling has much broader goals than merely helping a certain Kremlin's sister party at one or another election. One should remember that one of Russia's key long-term goals is to not only weaken, but to destroy the EU and NATO from inside. Simple erosion of democracy should be considered not less important goal of Kremlin's attacks.

Though the most publicised aspect of the Kremlin's direct support to one or the other political party as well as political leaders has been a financial one, the intellectual, informational and ideological assistance apparently in some cases can be as valuable and crucial. This is why fighting just 'fake news' and following the Kremlin's dirty money cannot solve the problem of Russian meddling in Western politics on its own.

Moreover, participation of Russian money in Western politics may well border on fighting windmills, if there is no serious and comprehensive international policy against dirty money in general, against the penetration of non-transparent Russian business into the West, and against enablers of such businesses.

A toolbox of support for the Kremlin-friendly parties is rich in measures, ranging between those widely believed to be just 'soft power' and real security service operations. However, it is also worth noting that Kremlin's efforts are certainly not limited to assisting marginal, anti-European and other non-mainstream political groups. That support cannot be seen in isolation from the contacts that it is building with traditional Western parties and politicians.

Quite often the Kremlin goes beyond supporting just one of the candidates. Even during one election or referendum, support can be rendered to different groups; actions by both marginal and traditional actors can meet the Kremlin's interests even in the framework of the same campaign. Therefore, long-term Kremlin support to traditional Western parties is worth as much attention and research and is as dangerous as its assistance to marginal groups.

On the other hand, not just the Kremlin's support measures should be taken into account. Kremlin is making use of its broad armoury of 'active measures' to ruin careers of politicians whom they dislike.

Having become a kind of the Kremlin's business card for its malign activities, cyber-attacks have been the main focus of discussions regarding Russian meddling in the elections and analysis of the ways of protection against the meddling. It needs to be remembered that cyber-attacks, regardless of their scale and nature, constitute just one method of malign information gathering (spying).

There is no reason to believe that it would stop using some components of traditional spying even now, in times of cyber-attacks. It is even more groundless to assume that, if there are no Kremlin cyber-attacks detected during one or another election campaign, or with no information available about a theft of essential information, the election can be deemed free of Russian meddling.

Going beyond one-country's effort is one of the important new aspects that should be taken into account when discussing and analysing Russia's meddling in Western elections. On the contrary, it involves an increasing number of transnational actors. Moreover, along with the 'active measures', well-known to Western intelligence, Russian election meddling practice is closely connected to financial and other crimes, and even involvement of the mafia. ■

The article is based on the study titled "A Guide to the Russian Tool Box of Election Meddling: a Platform to Analyse the Long-Term Comprehensive Kremlin Strategy of Malign Influence", conducted by Marius Laurinavičius for the Vilnius-based International Elections Study Center.

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WOLFGANG SCHARECK

# On the way to becoming a beacon of excellence in the Baltic Sea Region

Expert article • 2403

Six hundred years ago, the small seaport and trading Hanseatic City of Rostock had about 14,000 inhabitants. At that time Lübeck, the most important Hanseatic metropolis, had a population of almost 20,000 people. How could Rostock increase its prestige and attain more political and economic influence?

The aldermen of the Hanseatic City of Rostock recognized that in order to fill the need for merchants and traders, as well as teachers for schools and priests for the Church, it was essential for Rostock's economic development to educate their young generation in Rostock. Although first preparatory schools offering higher academic education already existed, the city lacked a university that could provide more than professional training. The secular lords of the City of Rostock did not have the authority to found a university; this was solely the privilege of the sovereign and the bishop. The approval of the Church was necessary. Thus, upon the petition of two dukes and chartered by the Papal Bull of Pope Martin V, the university was founded on February 13, 1419 with founding ceremony on November 12, 1419.

Universities established in the late Middle Ages were modeled after the University of Paris and the University of Bologna. This union of teachers and students was solely committed to knowledge and through the favor of the sovereign and approval of the pope, universities were a place of freedom from the feudal social system. Thus, a university was far more than an educational institution and gave their city high reputation. This was exactly what the up-and-coming Hanseatic City of Rostock needed. Already in the first years of the university's existence, it attracted not only students from Mecklenburg and northern Germany, but especially from the Baltic Sea countries and the Nordic realms, because it was the first university in the Baltic Sea region.

The small, late medieval university with initially 100 students (winter semester 1420/21) has after 599 years today become a renowned center of learning with almost 14,000 students. The University of Rostock is of course no longer the only university in the Baltic Sea region, but with its nine faculties it is one of the leading educational and research institutions and has approximately 250 professorships and an academic staff of more than 1000. The university is engaged in more than 1,100 third-party and especially funded projects and – with a third-party funding volume of 50 million euros – secures innovations and jobs not only for the present but also for the future. The favorable maritime location of the university, its

broad horizon of research activities, and its many patents, spin-offs, institutes and start-ups and even global players promise a continuous input of ideas, specialists and investments. For any research question, a unique scientific competence network can be accessed, which in turn is linked to a network of international scientists in the Baltic Sea region and worldwide.

The University of Rostock is no longer the only scientific institution in the city. Rostock could also be called a Hanseatic and Science City. Over the years numerous institutes have settled in the city, either as spin-off from the university or due to the favorable conditions of the location: one Max Planck Institute, two Fraunhofer Institutes, three Leibniz Institutes and one Federal Institute. Furthermore there is a Institution of Higher Education in Music and Theater. The university and the non-university research institutes together employ approximately 3,700 people.

The University of Rostock is not only a local beacon of excellence on a beautiful shore of the Baltic Sea. It is an international player in research alliances in the entire Baltic Sea region with over 1,000 cooperative projects and research topics focusing e.g. on coastal and environmental protection, an inland sea with estuary and lagoon, climate research, clean ship propulsion, recycling of finite resources and much more. These are all topics with regional, interregional and international significance that are highly relevant worldwide. They all increasingly require interdisciplinary cooperation in different fields of research. In 1951, the University of Rostock was the first in Germany to establish a Technical Faculty. Ten years ago, with the establishment of the Interdisciplinary Faculty, it took another decisive step towards the future. Today, the University of Rostock is pursuing the strategic goal of becoming one of the leading universities in the Baltic Sea region. ■

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PIOTR STEPNOWSKI

# University of Gdansk in Baltic Sea region

Expert article • 2404

**L**atin motto *In Mari via tua* defines well the University of Gdansk mission and its focus on the Baltic Sea as both the natural resource requiring protection and the geographical water basin offering opportunities for international cooperation within the principles of sustainable development. UG is an important center for Baltic Sea Region policy debates and analyses. The research is organized on land as well as at sea – the most innovative one can be carried out directly in the Baltic waters on the vessel *Oceanograf*. UG is also the initiator and the host of the National Centre for Baltic Research, which brings together local authorities and Pomerania's academic institutions. Its mission is to monitor and facilitate actions fulfilling the strategy set out as Polish maritime policy.

European Union regional policy in the Baltic Sea context singled out 4 pillars as fundamentally crucial: (1) to improve the environmental state of the Baltic Sea, (2) to promote more balanced economic development in the region, (3) to make the region more accessible and attractive, and, finally, (4) make it a safer place. UG's academic community operates often in interdisciplinary teams, participates in EU funded projects, shares findings at impactful conferences or by publishing research results in important journals.

UG's impact on environmental protection could be analysed in terms of both its research and educational activities. The latter could be best viewed in the context of all efforts by Baltic University Program. Researchers of UG are most quoted for their contributions on biodiversity in the Baltic Sea Region, algal blooming and all kinds of Baltic pollution threats. In 2018 UG hosted the largest Baltic congress on microbiology. Special emphasis was placed on participation of young researchers to introduce them to this field and give them an opportunity to learn from more experienced scientists.

UG is a leader in the project that facilitates sustainable tourism in cross-border dimension in Baltic Sea Region. It aims at construction and implementation 8 Heritage Routes and a package of 8 multi-day South Baltic Dream Tours. Based on unique concepts, sustainable – individual or small groups, environmentally friendly, respecting locality, the tours designed as part of the project will be smart and interactive. Each tour will be based on heritage route and will be tested by Exploration Trip. The strong involvement of tourism business to project activities will facilitate adoption of Baltic Sea Region tourist products in real business operations.

UG's contribution to the 4<sup>th</sup> pillar of EU Baltic Sea Region policy is about its engagement in multiple initiatives on developing democracy and peaceful collaboration of diverse cultures. In the Baltic Sea Region a transition to democracy and market economy has taken place after the systems change and Solidarity revolution in Poland.

University of Gdansk organized a number of seminars and student meetings on democracy as part of Baltic University Program. As all BUP UG's led initiatives contributed greatly to international contacts and it may be assumed that this is crucial for security. In most of exchange programs and short term residencies the emphasis was put on the students and their possibilities to get to know each other. It was possible thanks to bilateral agreements between universities and Erasmus Plus mobility.

From detailed analysis of the regional networks of higher education institutions in the Baltic States and the German federal state Mecklenburg–Western Pomerania it can be argued that a heterogeneous pattern for the regional higher education area emerges. Regional embedding depends on the focus of individuals within academics cultures and its participation in regional networks.

Similar pattern can be constructed from the research on social capital of University of Gdansk academic community. UG's community members and stakeholders in a focus discussion on the value of Baltic networks (BUP, BSRUN, BSN) identified resilience in relation to interpersonal and networking capacities sought by working life in the region. The key abilities included: active listening and responding

in order to contribute to unfolding professional interactions, non-defensive attitude and flexibility in the face of challenging intercultural problem solving activities.

Universities have a key role in the changes towards a democratic, peaceful and sustainable development of the region. This builds on a long tradition of internationalism within the academic world. It is extremely important for the youth of today that they are taught the values of life to prepare them for their future and for the future of our region. Today universities also address the general public, and cooperate with authorities and companies when specialist competence is needed. These roles of the universities are needed even more after the dramatic political and societal changes that have taken place in our region. ■

Universities have a key role in the changes towards a democratic, peaceful and sustainable development of the region.

PIOTR STEPNOWSKI

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ARTO RÄTY

# The Baltic Rim countries can lead the change for a cleaner world

Expert article • 2405

**E**U countries have committed to transitioning towards a more sustainable energy system in order to tackle climate change. The Nordic and Baltic countries are in a good position to lead the change, thanks to a common electricity market and a tradition of close collaboration. Yet much more could be done.

The implications of climate change, such as frequent occurrences of extreme weather, desertification, climate refugees and conflicts over basic commodities, have been well predicted for years and are already impacting our everyday lives also up here in the Nordics. The scientific evidence seems to indicate that we have already missed the ambition of the Paris Agreement to limit global warming to +1.5°C, and major actions are needed if we still want to stay within the +2°C limit. The current outlook is that the world is heading towards a devastating +3°C warming. I see this challenge as the gravest facing mankind today.

The EU Commission outlined a few years ago a roadmap towards a low-carbon economy by 2050 suggesting that the EU cut emissions by a minimum of 80% compared to the 1990 levels. But as we now know, this won't be enough for the +2°C limit; the Commission is indeed in the process of preparing a more comprehensive long-term climate strategy, possibly aiming for carbon neutrality by 2050. In this context, the Commission might also propose revising the only recently agreed 2030 greenhouse gas reduction target to put it on the right trajectory in relation to the target of carbon neutrality by 2050. The undertaking is huge and will require actions not only by the power sector, but by all the main sectors including transport, industry, buildings, construction and agriculture.

## Towards a carbon-neutral society

The power sector can contribute a lot to the transition, as clean energy technologies such as solar and wind power are quickly becoming mainstream and competitive on their own merit. The cost of solar modules has decreased by more than 80% since 2010 and wind turbines by over 30%. Of the total projected EUR 10 trillion investments in power generation by 2050 globally, over 70% are expected to be into solar and wind power. Consequently, these two technologies are projected to represent 50% of the global power generation mix by mid-century.

However, the power sector is responsible for only around 20% of the final energy consumption in Europe, while heating and cooling represent about 50% and transportation 30%. CO<sub>2</sub>-free electricity can help to decarbonise other sectors by replacing fossil fuels in traffic, heating and cooling, for instance, but the other economic sectors need to step up their efforts too. For example, currently less than half of the emissions in Europe are part of the emissions trading system. This exposure should be broadened to accelerate commercial investments in clean energy.

While it is completely plausible that power generation in Europe is largely decarbonised by mid-century, we are no magicians. The role

of politicians and regulators as enablers of an affordable and socially acceptable change is crucial.

## Commitment to collaboration

At Fortum, we see a highly-integrated and market-driven power market as a prerequisite for an affordable transition to carbon neutrality. The common Nordic power market – consisting nowadays of Finland, Sweden, Norway and Denmark, but also the three Baltic countries – has brought major benefits in the form of competitive prices, clean energy and excellent security of supply for all countries in the region. Backed by this leadership, the Nordic and Baltic countries could rightfully take a stronger position in influencing power market development in the post-Brexit Europe.

The changing energy landscape together with new technologies is nevertheless bringing new challenges also to the Nordic market. A number of issues should be addressed in the coming years in order to ensure that the Nordic power market can attract innovation and bring the same benefits for societies and customers also in the future, while helping to solve the climate issue in an efficient way.

First and foremost, the governments of the Nordic countries should commit to tighter collaboration and regular steering in energy issues – ideally guided by a shared vision based on competitive market design. This traditional Nordic cooperation should be genuinely opened up also to Baltic countries.

There is clearly room for more cooperation. For example, each country has recently outlined their national energy and climate strategies including the 2030 targets without any coordination with their neighbours. These decisions will have an impact on the whole market area. If one country in the same market decides on an ambitious national target for renewable energy increase, supported by a national subsidy scheme, it will impact the market balance in the neighbouring countries and in the whole regional market. The same applies to politically driven decisions to support or ban certain fuels or technologies. In an integrated market the impacts of national policies are not contained by borders. Therefore, it would be important to create a culture and institutionalise the practice whereby countries belonging in the same regional market would regularly exchange information on their national policy objectives and measures, and ideally agree on a similar regulation and taxation of energy.

## Making the most of our digital leadership

A requirement of a predominantly renewables-based and highly intermittent power system is that consumption is flexible. The Nordic countries have perhaps the world's most advanced digital capabilities, including smart electricity metering, that would enable consumers to actively participate in the market and function as a reserve. However, developing and rolling out products and services for an intelligent consumer market requires investments, which are not supported by the current national retail market structure. Harmonising the Nordic retail market is first and foremost a political decision, one that I believe

we should not procrastinate on.

Batteries are another source of flexibility and are especially suitable for short-term control. Industrial-scale battery installations complement hydropower and can be used to balance the power system within seconds. Development of common Nordic standards for flexibility markets should be made a priority, so that the Nordic countries can live up to the full potential of their digital leadership.

#### **Broader influence in the EU with a united front**

The need for transformation in the European energy system is unprecedented, but so is the climate challenge. The Nordic countries are in a strong position – thanks to an already largely decarbonised power generation structure, a tradition of close collaboration, good digital capabilities and a population that is willing to embrace new services. Other regions in Europe approach the transition from a less advantageous position and, quite naturally, want to secure their national interests. However, a national focus with non-market-driven mechanisms, such as capacity markets and lack of digitalisation, for example in the form of remote metering, will just delay change and increase the cost to society. A united Nordic and Baltic front with a clear vision and harmonised views of market development would strengthen our regional voice in Brussels.

If we do not lead the change for a cleaner world, who will? ■



#### **ARTO RÄTTY**

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KEITH MARTIN

# Nord Stream 2: A European project in the Baltic Region

Expert article • 2406

In Europe, Uniper contributes to supply security by moving towards a low-carbon energy future. A backbone for this is our midstream gas business which helps us to ensure gas supply through a diverse portfolio of gas contracts, along with gas storage, gas transport and liquid natural gas ("LNG"). For the German and European market, we have signed decades ago long term gas contracts for importing natural gas from the Netherlands, Russia and Norway. A further diversification of our gas portfolio is very important for us, and also LNG becomes increasingly significant to expand our commodity contract portfolio.

Gas is an indispensable element of Europe's future energy system and there is a natural symbiosis between gas and renewable energy sources. Gas is the efficient and low-cost solution for quick, yet lasting decarbonisation in all areas, be it in power generation, the heating sector or public and private transport. Gas is becoming increasingly important as a location factor for industry and will become even more important in this role, especially if Europe wants to achieve its ambitious climate goals. Today, Europe can still supply a large proportion of its own production with gas. But domestic production in Europe is falling faster than originally forecasted. At the same time, demand is rising. Above all, gas will replace coal and, together with the growth from renewable energies, will enable a climate-friendly and secure energy supply.

As an experienced energy undertaking, we have been importing gas from Russia since 1973. In times of declining European gas production, we believe that also Russian Gas has a competitive position and will play an important role in a diversified European gas portfolio in the long run. Therefore, a functioning and efficient gas transport infrastructure for gas from Russia is essential for European energy security. The Nord Stream 2 project will contribute to this. Uniper and other European energy companies are financing Nord Stream 2, of whose energy logic we are convinced.

Nord Stream 2 is a billion-dollar investment in state-of-the-art European gas infrastructure, in the secure supply of gas to people and industry in Europe. Nord Stream 2 will be a twin pipeline stretching 1,200 km through the Baltic Sea. Each line will comprise around 100,000 individual pipes, each 12 m in length. Nord Stream 2 will travel through the Baltic Sea, starting from the coast of Russia and reaching landfall near Greifswald in Germany. It will run roughly parallel to the existing Nord Stream pipeline.

Nord Stream 2 diversifies gas purchases and increases competition. It connects Western Europe directly and without any transit risks with the major Russian gas fields. Thanks to the well-developed intra-European gas network, Nord Stream 2 can also safely supply large parts of Central and Eastern Europe with energy. The Baltic Sea pipeline represents an important diversification of existing

import routes as well as a supplement to and extension of the existing network. This accords precisely with the aims of the European Energy Union and a strengthened internal gas market in Europe. Nord Stream 2 connects and strengthens Europe, it is a pan-European project in the very best sense. Many options always mean more competition. And several alternatives always mean more security. This will benefit European gas customers as well as the European economy.

Nord Stream 2 will pass through the territorial waters and/or the Exclusive Economic Zones of Russia, Finland, Sweden, Denmark, and Germany. Through the international permitting process, Nord Stream 2 will seek permits to construct and operate the pipeline from each of these countries. Other neighbouring Baltic states – Poland, Lithuania, Latvia and Estonia – are also to be consulted.

Also LNG imports to Europe can be one of the building blocks for security of supply, but they will not compensate for the anticipated shortcomings in Europe's gas supply. No "Either-or-Situation" shall arise regarding current or possible future energy partners. Existing partnerships have to be strengthened and new ones have to be developed further. For Uniper this also applies for the Southern Gas Corridor which will deliver gas from the Caspian Region and for future LNG-deliveries from the North-American-Continent. Nevertheless, future LNG or additional pipeline gas alone will not be sufficient to replace Russian gas supply into Europe in the short and midterm.

Russian gas supplies also in the future will guarantee supply security for Europe. As a partner to the major European employers, we as energy supplier have an obligation to ensure supply security and competitive gas prices. Russian gas supplies are an essential component of this. However, this is not about Europe's one-sided dependence on Russia, but about a partnership that has been ensuring very reliable gas supplies for several decades now. ■

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TADAS JAKŠTAS

# Maritime threats to energy security in the Baltic Sea region

Expert article • 2407

In the last couple of years, with growing tensions in the Eastern Flank of the Alliance, Russia has become more assertive in maritime disputes with its neighbours. Russia's provocative behaviour have included violations of national airspace and territorial waters, intimidation of planes and vessels in international airspace and waters, an increasing number of military exercises based on aggressive scenarios. For example, on several occasions in March and April 2018 the Russian Federation announced plans to conduct military exercises to tests naval-launched missiles in the Republic of Latvia's exclusive economic zone (EEZ) in the Baltic Sea. Subsequently, the Russian Federation's navy demanded to close part of Latvian airspace in an 18-kilometer altitude and 40 kilometres from Latvia's seacoast in an area of especially busy traffic for at least 36 hours. Sweden and Poland were also requested by Russia to close parts of their airspace for the missile tests. In similar incidents in 2014 and 2015, the Russian Federation navy while conducting military exercises disrupted civilian shipping in the EEZ of Lithuania and demanded the cessation of NordBalt undersea electric cable laying activities.

From the security perspective, Russia uses grey zone tools and techniques to achieve (geo) political objectives. Russia's goals suggest the need for grey zone revisionism as she seeks to renew Russian dominance of the near abroad, to undermine the North Atlantic Treaty Organization (NATO), and to coerce the foreign policy decisions of neighbouring states by using political, energy, and economic, and maritime intimidation in order to deny their right to align more closely to the West.

In addition, maritime disputes could have implications for energy security since economic cooperation in the region takes place mainly through maritime links, and there is a maritime dimension to almost every commercial activity in the region, including energy supplies. The Baltic Sea routes are used for exports as well as oil and gas supply diversification. In addition, the security of energy supplies could be disrupted by grey zone operations, including military activities, in the maritime domain due to fact that the Baltic Sea hosts some of the important regional energy infrastructure, including submarine cables (e.g. NordBalt, Estlink, LNG terminals).

In addition to security challenges, Russia's growing provocative behaviour in maritime domain raises important legal challenges for NATO and its concerned allies which have not been adequately addressed from the alliances' and individual member states' perspectives. Against the background of growing hybrid threats and grey zone incidents, current international law, largely the United

Nations Convention on the Law of the Sea (UNCLOS) mechanisms are not sufficient to ensure the security of critical infrastructure in maritime domain. Critical energy and communication infrastructure, including undersea cables, sea lanes of communication, maritime and air access to ports in Baltic Sea and North Sea could be disrupted by military activities, including naval exercises which might not be unlawful from the legal perspective domain but which could cause serious economic damage, safety hazards as well as to disrupt communication networks, limit or deny neighbouring states access to energy installations and resource extraction areas.

The security of critical infrastructure in the Baltic States faces a number of challenges. Some of the most critical nodes of energy infrastructure do not meet all physical security requirements. Moreover, there is a lack of intra-regional physical security exercises among TSOs in the Baltic States. In addition, there is a lack of regional exercises to test the ability to withstand a major electricity blackout scenario. The existing intra-regional cooperation in CEIP is not sufficient in the context of growing security challenges in the region.

The intraregional cooperation in energy security first of all is limited by the lack of awareness and understanding of the interconnectedness of threats in the region. The current cooperation on maritime security situational awareness and exchange of information is limited. The level and scope of cooperation within the framework of SUCBAS is not adequate, especially in the context of growing kinetic/non-kinetic threats in the region (e.g. aggressive exercises, dangerous overflights and maritime intimidation of vessels, increasing submarine activity).

In order to mitigate threats to sea lanes of communication and to ensure the security and safety of energy infrastructure in the maritime domain, the national authorities in the Baltic States should work together with the Nordic countries to address some of the following important challenges:

- Establish common coordination mechanisms to link maritime surveillance systems in the Baltic Sea Region in order to maintain 24-hour situational awareness in the entire Baltic Sea.
- Improve coordination and information sharing between national agencies, such as coast guards. In addition, national emergency response mechanisms should be integrated into regional response plans together with improvements in information sharing.
- Facilitate intra-regional cooperation to counter Russian threats and the legal challenges they present by creating a common intra-regional International Maritime Law Centre that could study, address, and respond to hybrid threats in the maritime domain.

The existing intra-regional cooperation in CEIP is not sufficient in the context of growing security challenges in the region.



Expert article • 2407

- Address incidents at sea before an unexpected escalation occurs by developing additional military-military crisis management mechanisms in maritime domain.
- Increase crisis preparedness by developing and testing contingency mitigation plans for partial/full closure of maritime areas of the Baltic Sea which could also affect energy supplies. Such plans should reflect the mitigation measures, including alternative land and sea lanes of communication. The necessary infrastructure and arrangements for fuel supply/re-supply and distribution operations should be tested in joint regional civilian-military exercises.
- Improve regional maritime training focusing on the most effective counter measures against the intentional/unintentional loss of GNSS signals.
- Develop intra-regional cooperation and share the best practices in raising cyber security awareness among the personnel in energy sector. ■

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MIRIAM HOLSTEIN

# Open innovation is the key to success also in the Nordic region

Expert article • 2408

**O**pen innovation – the idea that companies can greatly benefit from tapping into knowledge sources beyond their internal R&D operations when developing new products and services – has gained global momentum since it was originated by Professor Henry Chesbrough around the turn of the millennium. A great deal of current scientific endeavor and technological development is based on sharing the risks and rewards of costly innovation activity through the open innovation model.

## Expertise is everywhere

The days of global companies trying to invent the wheel in isolation are gone. The world we live in is increasingly complex and intertwined. Valuable knowledge and expertise is distributed everywhere: among individuals, patients, customers and end-users, academia, public agencies, startups, suppliers, investors and our competitors.

There has also been a clear change of mindset regarding innovation during the past few decades; a recognition within companies that internal expertise is not sufficient to fulfil our business and innovation objectives, nor the wider role we wish to play in shaping the future wellbeing of society. The open innovation approach has proved to be fundamental to addressing the major challenges of our times, including global health and food concerns.

## Innovation-friendly environment

The Nordic region offers one of the most innovation-friendly environments in the world. Although there are differences between the Nordic countries, many comparative studies have pointed to common factors like the high level of education, the share of GDP spent on R&D activities, and the high number of researchers and scientists as contributing to the innovation strengths of the region.

My observations focus on the Finnish innovation context because I started in my role at Bayer Nordic's headquarters in Espoo, Finland, in September 2017. The openness of the Finnish health ecosystem has been one of the first things to make an impression. The mentality here is very collaborative and less hierarchical than in Germany for example. This helps to create new opportunities for joint innovation activities. In that context, it has also been rewarding to see the lasting impact of the effort made by my predecessor in bringing together the different actors of Finland's lively health ecosystem.

## Attractive innovation strengths

Finland is consistently ranked among the world's most innovative economies. The availability of highly educated personnel is of utmost importance for companies. For pharmaceutical companies one of the pull-factors has proven to be the access to Finland's national healthcare registers and data, enabled by biobank legislation that supports innovation activity.

Bayer has established strong collaboration with Finnish biobanks, universities, university hospitals, ministries and other governmental stakeholders as well as innovative Finnish companies. The availability of highly educated personnel is a key reason why Bayer Group's fourth largest global clinical research unit is located in Espoo, Finland, and why our R&D unit focusing on polymer-based drug delivery technology is based in Turku, Finland.

Locally, we have recently partnered with the University of Turku and Bayer is one of the seven companies participating in the newly established Laboratory of Business Disruption Research. The objective is to strengthen our capacity to develop new business models and readiness to address new challenges.

Bayer's global long-term approach to innovation is called Leaps by Bayer. It includes major venture capital investments in key areas like DNA editing, microbiome, RNA inhibition, RNA activation and cell stem therapy. The aim is to conquer ten huge challenges facing humanity by making paradigm-shifting advances in the life sciences. Innovation of this magnitude requires new levels of investment, risk and trust that go beyond conventional limits in the healthcare and agriculture industries.

Innovation is a journey. In the case of pharmaceutical research this often takes many years, yet the first spark of inspiration always ignites at the local level. At Bayer Nordic, we aim to be one of the most innovative regions within the Bayer Group: the ideal place for test bed and pilot projects to develop new products and solutions for the global market. This is the reason why we are strategically committed to active collaboration at all levels of the Nordic health and agricultural ecosystems, facilitating and nurturing the innovative spirit of this region. ■



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EVGENY LEBEDEV

# Belarus-Finland investment cooperation

Expert article • 2409

In the past five years there has been a remarkable increase in inward foreign investment stock in Belarus which is very close to \$20 billion. According to United Nations Conference for Trade and Development this indicator grew by more than 30 per cent from the beginning of 2013.

Traditionally Finland is among top-20 most active investors in Belarus. However, recently the number of companies with Finnish capital here has slightly decreased. So did the amount of investment from Finland (from \$22 million in 2015 and \$18 million in 2016 to \$13,6 million in 2017).

It is important to note, that this negative trend has objective reasons. Firstly, the investment cooperation of Belarus and Finland is inevitably exposed to global processes. According to UNCTAD World Investment Report global flow of foreign direct investment (FDI) has decreased by 23 per cent in 2017 and the distribution of foreign investment to transition economies, such as Belarussian, fell by 27 per cent comparing to the level of 2016. Secondly, there is a general trend that shows the reduction in Finnish outward investment, which is characteristic not only of cooperation with Belarus.

Apparently in current global investment environment competition intensifies among donors and recipients of FDI as investment is one of the most important forms of capital placement and a key factor of economic growth for developing countries.

Despite the global trends, it seems that there is a favorable situation today, which can contribute significantly to the development of investment cooperation of Belarus and Finland.

Previously one of the main obstacle to invest in Belarus was lack of awareness of foreign companies about business environment in our country and their tendency to exaggerate possible investment risks, related to the activity in Belarus. Present improvement of the situation is stated by such authoritative rating agencies as Fitch and Moody's. They improved the credit rating of Belarus to B, stable outlook.

After the updating of the Organization for Economic Cooperation and Development (OECD) Country Risk Classification on January 26, 2018 the position of the Republic of Belarus was improved for the first time since 1999. Our country was reclassified to the sixth group. In practice the improvement of the position of Belarus means that credit risks have reduced significantly in the country.

According to the World Bank country rating on the key aspects of legal regulations of business activities for national companies (Doing business-2018) Belarus ranks 38<sup>th</sup>, while in 2006 it ranked 106<sup>th</sup>.

One of the most important steps towards improving business environment in Belarus recently was the adoption of a Decree №7 "On the Development of Entrepreneurship". In accordance with its provisions the registration procedure for business entities and the way for their cooperation with state bodies has been simplified, a moratorium on the tax legislation changes was introduced until 2020,

the interference of state bodies into the activities of business entities was minimized, the requirements for environmental protection were systematized.

It is possible to overcome the negative dynamics and to strengthen the mutually beneficial cooperation of Belarus and Finland through the participation of Finnish business in the already existing projects.

One of the most successful projects aimed at attracting investments is the High-Technology Park (HTP). The highest increase in number of HTP residents and the amount of export of services has been observed here in 2018. In January-September of this year 200 new companies have been registered in the Park. Thus, in less than a year there have been more new companies than in the past 12 years. In 2017 export of HTP increased by 25 per cent and for the first time has reached the level of \$1 billion. What is more, during the first half of 2018 the increase in exports, without including the new companies, amounted to 40 per cent.

These results were accomplished first of all by virtue of coming into effect of the Decree №8 "On the Development of Digital Economy" on March 28, 2017, which is aimed at liberalization of entrepreneurship in IT and the development of high-technologies.

Chinese-Belarusian industrial park "Great Stone" can become another key project for investment cooperation. Its building started in 2014 and the first production plant opened on September 5, 2018. The residents from any country can enjoy huge tax privileges such as the reduction of income tax rate or exemption from customs fees on industrial equipment. In addition, the investor will be able to sell its products to EAEU-countries (more than 180 million people) without import duty.

Belarus has a constructive investment policy. In recent years favorable conditions for large-scale productions as well as for small and medium business have been created. Therefore, now Belarus and Finland have all preconditions not only to reactivate, but to improve their investment cooperation. ■

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GALINA GRIBANOVA

# Russia-NATO confrontation on the Baltic Sea

Expert article • 2410

There are no doubts that the Baltic Sea is of special geopolitical significance both for Russia and a number of European countries – NATO member states and those that keep their neutral status. On one hand, the military forces of the NATO Alliance and that of the Collective Security Treaty Organization (CSTO) contact here directly. On the other hand, the importance of the Baltic region regarding global economy, trade development and the direct access to the World Ocean is beyond any controversy. Even during the Cold War the ruling elites of the countries in the Baltic region strove to follow the slogan “The Baltic Sea is a Sea of Friendship.” During the Cold War the American policy toward the Baltic region was built on containment of the USSR by strengthening allies and exerting pressure on neutral countries such as Sweden and Finland. This was being done both openly and behind the scenes. In the President Ronald Reagan era, the focus was not on the Baltic region per se, but rather on the countries along the borders of the Eastern Bloc. After the fall of the Berlin wall and the withdrawal of Russian troops from Lithuania, Estonia and Latvia, the Baltic States joined NATO and the Baltic region was considered to be one of the most peaceful places of the world. But now, especially after the Ukrainian crisis, we can see here a visible growth of tension between NATO and the Russian Federation.

According to the NATO basic official documents the explanation of the military presence escalation in the region is the necessity to defend the Baltic countries from Russian threat. The main concern is about the fact that, from the military point of view, the Baltic States that are now considered to be the next target for Russia's aggression on the post-Soviet territory are isolated from other NATO members.

It is difficult to say for sure whether the NATO strategists really believe in the existence of the Kremlin “Crimea scenario” for Estonia, Latvia and Lithuania or they simply use this idea to justify their actions for dragging the neutral North European states into NATO. In fact, for us the huge difference between Crimea and the Baltic States seems obvious. Certainly the Russian authorities use the situation with the Russian-speaking population of these countries in propaganda but the RF has a lot of much more urgent problems to resolve. No sane politician will dare to risk the involvement of the Russian army into direct confrontation with NATO without very good reason. And in today's reality such good reasons do not exist.

The most dangerous in this situation for Russia and for the security of the whole Baltic Sea region is just these attempts to encourage Finland and Sweden to join NATO, to press ruling elites of these countries to change their neutral status. If it happened the expansion of NATO to the East would be supplemented by its extension to

the North. It is certainly a great worry for Russia and, first of all, for its bordering regions with Finland - the Leningrad Oblast and the Republic of Karelia as it will not only increase tension in the region, but also inevitably lead to significant additional defense spending by the RF.

In any case the key role in making decision about NATO will be played not by the U.S. but by public opinion and the political elites positioning in the Nordic countries. It is difficult to predict whether Sweden will make any practical steps in NATO direction as the new government hasn't yet been formed. As for Finland, the government is against immediate seeking NATO membership but has kept the option open. Let's hope that pragmatism and the common sense, so characteristic of Finland foreign policy for decades, will help the ruling elites of the country not to yield to NATO leaders' pressure.

We are sure that the increasing military confrontation on the Baltic Sea does not answer the interests neither of the European Union, nor of Russia, and the very atmosphere of mutual distrust and suspicion creates the greatest threat. In this situation Russia should intensify the information efforts to explain its position with regard to the most acute problems in relations with the Baltic countries, Sweden and Finland in order to prevent speculations about the real interests of the RF in the region, to expose the myth of hybrid war preparation against the Baltic States. The military rhetoric on the part of NATO strategists, accompanying the discussion of any topics related to Russia, should be a concern not only to Russia, but to other Baltic countries, the most reasonable groups of the Baltic States political elites that are aware of the danger of escalating tensions in the region. Only in this case it will be possible to hope for the opening of a certain “window of opportunity,” if not to improve, but at least to stabilize relations between Russia, the Baltic countries and NATO in the Baltic Sea region. ■

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IVAN KURILLA

# US – Russian relations as international manifestation of domestic culture wars

Expert article • 2411

**C**urrent pity state of the US- Russian relations cannot be explained by the development of the system of international relations. Indeed, the conflicts in Ukraine and Syria are grave but it is hard to compare them to the Cold War era wars like Vietnam or Afghanistan; there is no more international military political organization to balance NATO as Warsaw pact was; yet, the hostile rhetoric in both Russia and the United States had surpassed the Cold War examples.

To understand the situation, we should see it in the context of the domestic culture wars unfolding in the both countries. Russia and the United States for many decades played for each other the role of "constitutive Other", the nation to compare, juxtapose and surpass in their own way to the brighter future. During every domestic crisis the attention to the US in Russia or Soviet Union increased; the same is true for the American discussions on Russia. More often, the crises in two countries were not simultaneous, as the 1970s problems in the United States (with the abandonment of the détente by the Carter administration) or 1990s dissolution of the USSR (with its swing from love to hate toward the US in Russia).

However, we see the simultaneous crises of identity or culture wars unfolding both in Russia and the United States in the recent years.

In Russia, the culture conflict was provoked by the state in the aftermath of the public protests in the winter of 2011-2012. The improbable alliance between nationalist and liberal opposition against the government scared the Kremlin, and soon after presidential election in March 2012 it introduced a shift towards "traditional values". It included the increase of the public role and influence of the Russian Orthodox church and state protection of the most conservative social groups. The most important milestones of the shift were the "Pussy Riot" trial (2012), law against "publicly offending the feelings of believers" (2013), law "for Protecting Children from Information Advocating for a Denial of Traditional Family Values", also known as "gay propaganda law" (2013), and decriminalization of domestic violence law (2017). The policy change provoked the split within Russian society most of which is not traditional in any way, and the annexation of Crimea in 2014 added the emotions into the domestic battles between the "conservatives" and the "liberals".

The attitudes toward the United States was the important part of the shift. While the anti-American feelings were steadily growing since NATO bombing of Yugoslavia in 1999, the Kremlin accusations of the US meddling into Russian domestic politics emerged at the peak of the protest in the winter of 2012. In order to marginalize Russian opposition leaders state propaganda claimed that their contacts with the Americans were the proof of their anti-Russian activity. Such an accusation involved redrawing the image of the United States that since that point was portrayed as a demonic power aimed at

undermining everything Russian. Demonic image of America helped propaganda to rally core supporters of the Kremlin around the flag and to alienate opposition. Moreover, Kremlin announced Russia to be the worldwide champion of the traditional values, as opposing to the United States proliferation of liberal values.

The culture war in the United States took its most aggressive form since the 2016 elections of Donald Trump to the office of President. Democratic critics of Trump consider him an embodiment of the everything liberal America oppose; sexism, racism, political incorrectness and so on. The recent examples of the culture war turned to violence were race riots and Confederate monuments removal in 2017. The opponents also claim that Donald Trump was elected into office because of the Russian meddling into American elections, strangely mirroring Kremlin propaganda of 2012. Whether Russian meddling was so important as to influence the election outcome or not, the focus of the domestic conflict in America was diverted from the home division and the failures of the political establishment to the foreign interference. Cold war rhetoric easily replaced analysis in the publication of the leading US newspapers.

Not surprisingly, Donald Trump also considers Russia as a rhetorical battlefield rather than the real country with its own concerns. For him, any breakthrough with Russia would turn the domestic culture war into victorious road. Trump wants to follow the example of Ronald Reagan who changed the image of the Soviet Union during his meetings with Mikhail Gorbachev and thus delivered America from the fear of nuclear war and won additional sympathies of the Americans. However, Trump attempts at rapprochement with Russia falls apart because of the high intensity of anti-Russian suspicions in the United States. The July 2018 Helsinki summit was not a success due to the domestic outrage of the very possibility to make deals with Putin.

As it always happens during culture wars, Russian-US relations fell victim of the domestic concerns in two countries. Such an approach also means that no international development could influence the state of the US-Russian relations. Domestic development in one or both countries can do the job. ■

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MARCIN KACZMARSKI

# Russia and China: fellow travellers

Expert article • 2412

There could hardly have been a greater contrast between Xi Jinping awarding the first-ever Friendship Medal to Vladimir Putin and the Western leaders quarrelling with Donald Trump at the G-7 meeting last June. But just as true and grave are the West's fault lines, so illusory is the unity of the non-Western world. Neither SCO, nor another grouping, BRICS, share a joint vision of how a future international order should look like. Moreover, the Sino-Russian relationship, which remains the glue of both SCO and BRICS, is permeated with serious limitations and cannot serve as a foundation for an alternative world order.

At first sight, Moscow and Beijing share similar worldviews. Russian and Chinese ruling elites feel entitled to a privileged position and emphasise unique global roles they play, especially when it comes to international security and conflict resolution. Both cherish the traditional 'Westphalian' definition of sovereignty, which they understand as the state's impunity within its borders. At the same time, Moscow and Beijing continue to pay lip service to the primacy of international law and declare the UN to be the most important global institution. Behind their repeated calls for 'democratization' of international relations, Moscow and Beijing express their shared desire for a diminished role of the Western states, the US in particular. This similarity does not, however, equate long-term convergence. Their ultimate destination is far from being identical.

The biggest challenge for the Sino-Russian relationship is the growing asymmetry between the two states. The gap between the two states' material power – measured in terms of GDP, trade, investments, and military budgets – has steadily increased to the advantage of China.

Secondly, due to worsening ties with the West Russia needs China's support more than vice versa. Neither Trump's presidency, nor growing backlash against Chinese influence from Australia to Western Europe, have not changed this basic equation. Despite numerous attempts to mend ties with the Russian leader and a strong desire to wage a trade war against China, Trump's policy has not strengthened Moscow in its dealings with Beijing. The West no longer casts China as a prospective responsible stakeholder vis-à-vis Russia being an international spoiler. Instead, the trans-Atlantic establishment gradually considers both states to be playing in the same league.

One reason for Moscow's failure to diminish power asymmetry with China is an objective weakness. Russia cannot offset Chinese losses, such as the reduced Chinese goods and capital access to Western markets and technologies, or the closure of avenues for China to influence the Chinese diaspora. China was able to compensate Russia for part of the losses the latter incurred as a result

of Western sanctions after 2014. Even if Beijing's economic support for Moscow had been limited, China had the potential to grant Russia a lifeline. Russia cannot return the favour.

Final and the most important aspect of the asymmetry between Russia and China concerns their varied engagement with global economy and related stakes in its future. Beijing supports economic globalization and market openness. As a result, it remains interested in stability and predictability on the global scale. The weakening of the West and the US plays into China's hands, but the power transition needs to be incremental. Russia, in turn, is less integrated into the global economy and its elite feels that the liberal order has not benefitted Russia at all (it certainly benefitted many of its members, though). Consequently, the Kremlin thrives on chaos and unpredictability. It cannot be sure how a certain crisis, be it Brexit or Catalonia's independence referendum, may benefit it, but it can at least open up certain possibilities to broaden Russian influence.

Under these conditions, a new special relationship emerges, with Russia becoming a junior partner and de facto accepting China's leading role. Moscow's diplomatic activity, the invention of new strategic concepts such as Greater Eurasia, and demonstrations of amity between Putin and Xi will certainly help to hide this asymmetry behind the curtain of equality. One reason why Moscow is ready to accept such a role is regime security. China's rise does not threaten the Kremlin's grip on the Russian society. China will do nothing to undermine Putin's position. Besides, China has been careful to demonstrate ritual respect for Russia's great-power sensitivity and to exercise self-restraint in those areas where it has gained an upper hand, for instance in Central Asia. At the same time, China may learn that junior partners can be troublesome. Beijing may one day be forced to limit damage that Russian actions may have on global stability. In such a case, two scenarios are most plausible. Either Russia mitigates its behaviour due to China's pressure, or both states will gradually diverge. ■

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MARK D. STEINBERG

# The Russian revolution in prison: When history matters

Expert article • 2413

I have been teaching history in a medium security men's prison in the state of Illinois for two years as part of a program that organizes university courses, individual tutoring, reading groups, and other activities not only to benefit individuals but also to "demonstrate the positive impacts of higher education upon incarcerated people, their families, the communities from which they come, the host institution, and society as a whole" (from the mission statement of the Education Justice Project). Most of these students were convicted of crimes that carried sentences of many years, often decades. In this essay, I reflect on what teaching a course on the Russian Revolution in prison taught me: about pedagogy, about the social value of humanistic learning, and about understanding the past. By extension, these reflections raise questions about the world of today in which inequality and injustice are still all too common.

In my centenary course on the Russian Revolution, we read scholarly histories, including my own new book, *The Russian Revolution, 1905-1921*, and especially primary-source voices from the past, including both the major leaders (Lenin, Trotsky, Kollontai, and others) and ordinary men and women: workers and peasants, soldiers and sailors, writers and intellectuals. These students, with one exception, an autodidact intellectual, knew almost nothing about Russia apart from some fragmentary impressions about Stalin, World War II, and the Cold War and what was said on television news about Putin and Russia today. To be sure, most of my university undergraduates know little more. But where these incarcerated men differ dramatically from the typical nineteen-year old college student is the depth, complexity, and harshness of the life experiences they bring to their study of the past.

These men are trapped in a dull and limited world, where learning is a momentary escape. Many of them have a great passion for the life of the mind and a great belief in critical thinking as the first attribute of a citizen, even as a type of freedom. Like most professional historians, I do not believe that learning about the past is mainly about how many facts one can absorb or even the pleasure of encountering interesting new stories about other times and places. "Learning" involves much more, including connecting past stories and lives to our own lives and times and nurturing critical analysis of past and present. It is not just that those who forget the past are doomed to repeat it, as the old saying goes, but that the past is a treasure of knowledge about our shared humanity in all its variety and thus a tool to help us critically understand human society.

These incarcerated students understood, often instinctively, that history matters most when it touches both intellect and emotion. Emotions are a difficult terrain for scholars. Yet revolutions are times of great emotion. In Russia, as a centuries-old order collapsed and the state came into the hands of radical visionaries believing that they were taking Russia and humanity on an unprecedented journey toward a "new world"—and I would argue that most revolutionaries sincerely believed that—people encountered a flood of feelings

in themselves and others, ranging from hope to fear, from joy to anger, from enthusiasm to disappointment. My students were often skeptical, especially as the class began, whether there was anything in an exotic history that unfolded a century ago in a distant country that would matter to them. To be frank, one student left the course because he could see nothing worth his time—and the course was demanding, requiring many hours of reading, weekly writing, and a three-hour discussion every week. But most of these students came to recognize in the past stories that were uncannily familiar, especially at the level of human experience, including the emotional toll of being poor and subordinate, ubiquitous violence in one's community and coming from the state, the madness of the crowd once aroused, and persistent dreams of freedom and a new life.

Students pondered the varied ideas, hopes, and disappointments that animated the revolution. They were most attracted (as I am as a researcher and teacher) to "experience": how people made sense of events and choices; the role of belief, faith, and desire; emotions entwined with ideas. Stories about different groups and individuals—ranging from peasants in the village to rulers in the capital—were found to be windows to explore the weightiest issues of the Russian past, including justice, freedom, power, and democracy. And every time we talked of these matters, we thought about their meanings through the prism of our own lives and our own social worlds. At the same time, students became increasingly aware of the complexity, contradictoriness, and even ambiguity of history. At first, students were dismayed by the "madhouse" (as one student put it) of the revolution and felt confused and lost in all the disorder and multiplicity. But in time, they saw truth in their first reaction. This recognition of intense complexity also meant eschewing simple moral lessons about who is good and who is evil in difficult times. And it meant recognizing how people with different experiences—women, non-Russians, workers, soldiers, peasants, intellectuals—differently understood contested ideas such as democracy or justice. This was an insight into the history of the Russian Revolution, but also an insight into the present as well.

In his final paper, one student concluded that studying the Russian Revolution was "a search into humanity, theirs and my own." It is not surprising that men in prison continually returned to the question of what it means to be human and to be recognized as human—a key theme in the Russian Revolution as well. Experiencing deep personal histories of humiliation and indignities (most of these men are African-American or Latino and all are working-class) encouraged attention to comparable experiences in Russia of a century ago. They were especially interested in stories about soldiers and sailors, people of the streets such as prostitutes and hooligans, and other subalterns, but also rebels of all sorts. On the other hand, they were deeply suspicious of people in authority, particularly Lenin. Desiring a life in which their humanity is respected, including by themselves, is what some students told me motivated them to participate in college

Expert article • 2413

programs in prison. Freedom, they perceived, requires a life in which human dignity and capacities are encouraged and thrive. Getting out of prison will not alone make them “free” any more than the end of tsarism, expelling aristocrats and capitalists, or breaking down prison walls made post-revolutionary Russians free. These students admired the humanistic passion for justice and change in the Russian revolution. But they also saw revolutions as a times of chaos, violence, and cruelty, which often fail in their emancipatory promises. Through the prism of their own lives, they understood a great deal about the Russian Revolution itself and about why it still matters. Their insights have much to offer us. ■

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**BALTIC RIM  
ECONOMIES**

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OLAVI ARENS

# Brest-Litovsk in retrospect: A hundred year

Expert article • 2414

**W**e have been living through a spate of 100-year anniversaries. Among them are:

1. The outbreak of World War I – 2014
2. U.S. entrance into the Great War – 2017
3. Russian Revolutions – 2017
4. Declarations of Independence by the Baltic States – 2018 (Finland 2017)
5. Paris Peace Conference and its treaties – 2019
6. Peace treaties between the Baltic States and Soviet Russia – 2020

Yet there was one 100-year anniversary that has been comparatively unremarked and certainly not celebrated – the Treaty of Brest-Litovsk between Soviet Russia and the Central Powers signed on 3 March 1918. The Treaty and its companion treaty with Ukraine marked the beginning of a process to end the war in Europe in which the Treaties of Paris were only a way-station. Peace was finalized by a number of separate treaties in Eastern Europe that taken together established a new political order in the eastern Baltic region. In fact the issues at the Brest-Litovsk negotiations: establishing peace, defining national self-determination and national minority rights, and containing the Bolshevik Revolution or conversely limiting German gains, were all issues with long-term implications for the 20<sup>th</sup> century.

At Brest-Litovsk the German Foreign Minister, Richard von Kühlmann, justified the separation of Poland, Lithuania, and Courland (the areas of the Russian Empire occupied by German and Austrian troops) in terms of self-determination that was exercised in the case of Courland by the historic Landtag of the Baltic German nobility supplemented by a few co-opted Latvians. Trotsky, in accordance with Lenin's formulation in the Decree on Peace, countered by advocating a referendum that would be preceded by a German military withdrawal from the territory. He pointed to the example of Finland where an elected Diet of an unoccupied country had voted to declare independence. The Soviet Russian government recognized the independence of Finland shortly afterwards. Similarly, Trotsky offered that, following a German withdrawal from the parts of Latvia and of Estonia (the islands) that it occupied, the Soviets would allow the remaining parts of Latvia and Estonia to participate in referenda on their future status. Since the German side knew they could not win an election, Kühlmann did not support an election. As the Estonian

Constituent Assembly elections showed in January 1918, neither could the Bolsheviks win an election.

As the negotiations came to a deadlock, the Germans responded by occupying the remainder of Latvia and Estonia in February 1918. Within the confines of a German military administration, the Baltic German aristocracy was allowed to construct the framework for a new political entity (Baltic Duchy) that was to be tied to Germany. The British and French reaction to Brest-Litovsk was to extend de facto recognition in May 1918 to the Estonian Diet that had been elected in 1917. The negotiations had internationalized the Baltic issue.

In conclusion what the Brest-Litovsk talks and the Treaty showed was that the major powers were willing to consider the separation of what became the Baltic States from Russia. Germany was willing to recognize and support the establishment of a Baltic as well as a Lithuanian Duchy tied to itself. The new Soviet Russia theoretically was willing to sign a peace treaty that accepted the idea of a referendum that could lead to the separation of the area from Russia. The Entente states also showed a willingness to consider Baltic independence. The empire built by Peter I, Catherine II, and Alexander I in a hundred-year period (1721 – 1815) that brought the area into the Russian empire had collapsed. An entirely new political order emerged in the eastern Baltic with an independent Finland, Estonia, Latvia, Lithuania, and Poland. Brest-Litovsk played a role in bringing it into being. ■



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# Russia's external debt

Expert article • 2415

The size and dynamics of external debt are two very important macroeconomic indicators of the health of an economy. They provide a measure of its financial stability and of the flow of resources into the economy from abroad, both of which make an essential contribution to, among other things, economic growth. Up until 2008 the vigorous growth of the economy of the Russian Federation was accompanied by a rapid accumulation of external debt. The global economic crisis of 2008-2009, which resulted in a significant fall in oil prices and to a massive outflow of capital, brought this accumulation of external debt to a halt. There was a resumption of growth in external debt from 2012-2014 but this was interrupted by another crisis. As a consequence of a twofold fall in the nominal exchange rate of the rouble relative to the US dollar and of the debt repayment whereas opportunities for the attraction of new loans became fewer, the total external debt fell by approximately 200 billion dollars over a period of two years, or by almost 30%. At present external debt is at the level of ten years past.

Hitherto, the largest share of the Russian external debt had consisted of the debt of the private non-financial sector. The public debt of the Russian Federation during the entire period under consideration was not high and on 1 July 2018 it did not exceed 50 billion US dollars. It should be noted that, whereas sovereign debt is formally at a low level, the substantial participation of the state in the Russian economy has created a situation in which the external debt of companies in which the state owns over 50% of the capital is high. If one includes companies controlled by the state, the external debt of the state sector as broadly defined is 255 billion dollars, or 49% of total external debt, compared with 77 billion US dollars (15% of total external debt) in the case of state owned institutions and the Central Bank. This means that many of the largest Russian companies are bearing a lower risk premium, or one that is close to the sovereign risk premium for the Russian Federation.

Debt duration is its important feature. According to data for 1 April of this year, out of 520 billion dollars of external debt 28% was subject to payment on demand, 89 billion dollars were payable in 1 years, 51 billion in between 1 to 2 years and 284 billion in periods over 2 years. For understandable reasons, the external debt of the Bank of Russia has the shortest payment schedules and the public external debt has the longest: the share of debt payable in over 2 years in the total indebtedness of this sector exceeds 93%.

An analysis of the currency composition of external debt reveals that at present approximately one quarter is denominated in roubles. This proportion did not greatly alter during the period under consideration. It has decreased in periods when the rouble has weakened and subsequently it has increased.

In any analysis of external debt the question of its sustainability is crucial, since an exorbitant level of external debt, and/or significant expenditures on debt servicing have often been a cause of crisis in developed and developing countries. However, in the case of Russia these indicators are entirely favourable. Thus, the ratio of external debt to GDP and to the export of goods and services at the end of the first quarter of this year did not exceed 32% and 120% respectively, which proportions by international standards are not high and which, if one applies the thresholds of the International Monetary Fund constitute an average level of risk. However, as we have already mentioned, Russian external debt is relatively short term, and the ratio of external debt payments to GDP and to the export of goods and services for next year amounts to 8% and 32% respectively. This represents a high level of risk. However, if one takes into account Russia's substantial international reserves, which exceed by three times the value of annual external debt payments, Russia's external debt is entirely sustainable and provides no cause for anxiety.

It is important to understand that funds provided by non-residents can be an important source of investment finance and of economic growth. Given the need to increase the rates of growth of the Russian economy to a level exceeding the world average, and given the limits of domestic resources, foreign borrowing must be considered indispensable. From this point of view, the stagnation of foreign lending in recent years is an

unpleasant indication that non-residents are reluctant to fund Russian companies in conditions of slow economic growth and an increase in geo-political risks, and also of the absence of new, profitable, investment projects for which Russian economic agents would be willing to borrow from non-residents. ■

It is important to understand that funds provided by non-residents can be an important source of investment finance and of economic growth.

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ALEXANDER BULATOV

# Offshore orientation of Russian FDI

Expert article • 2416

The article uses the term “offshore orientation” with respect to foreign direct investment to describe a large share of tax havens, offshore financial centers as well as transshipment countries (jurisdictions through which large volumes of FDI transit, e.g. Luxembourg, Ireland, Austria, Switzerland, the United Kingdom, the Netherlands) in FDI flows. In this sense, all countries participating in FDI are “offshore oriented” to a certain extent. For instance, in 2017 about 21% of Latvia’s FDI accumulated abroad and about 33 % of FDI accumulated in Latvia were “offshore oriented”, in Sweden the corresponding figures in 2014 were 26% and 56%. However, the FDI of the leading developing economies are more oriented (in comparison with developed economies) towards offshore entities and transshipment countries. In 2013 in China not less than 73% of FDI outflow and 78% of FDI inflow were “offshore oriented”, in Russia the corresponding figures were 90% and 91% in 2017.

Traditional explanations of developed economies’ FDI orientation towards offshore entities and transshipment countries cite tax planning motives. In developing countries, these motives are supplemented by non-traditional motives (push-out factors) – insufficient safeguards for legal business, poor levels of financial market development, high incidence of monopolization. In other words, negative elements of the investment climate generate additional, non-traditional motives for an “offshore orientation”. All these motives (factors) are typical for Russia and other leading developing economies. The latest World Economic Forum annual report measures the property rights protection in Russia in 3.6 points and in China – 4.6 (Finland – 6.6), financing through local equity market in Russia– 3.1 and in China – 4.5 (Sweden – 5.4), intensity of local competition in Russia – 5.0 and in China – 5.5 (Germany – 5.9).

It is not surprising that under these circumstances Russian investors export capital to, for instance, Cyprus, British Virgin Islands in great volume. They do so not only for the low local corporate tax but also for the possibilities of applying to the local courts in cases of violation of the company’s rights in other countries – including their native countries – and of lodging an appeal with the Judicial Committee of the Privy Council in London, for instance. For these reasons, the majority of leading private companies in Russia are de jure owned by firms or funds from offshore entities or transshipment countries. Of the 50 top private companies of national origin (which produce

one quarter of Russian GDP), 23 are of these type. Consequently, Russian companies and banks use their offshore affiliates to reduce transaction cost when placing their securities in the financial markets of the UK, the Netherlands, Luxembourg, Switzerland. At least five leading Russian banks have affiliates in Cyprus, as do numerous financial and investment affiliates of other Russian parent companies. Also high level of monopolization and oligopolization of Russian economy leads to the high cost of entry to many local industries and national investors have to go abroad, particularly to offshore jurisdictions.

It is worth noting that the principal volume of this “offshore oriented” assets returns back to the country of its origin. Indian, Chinese, Russian statistics states that geographical destinations of FDI outflows and inflows coincide in general. For instance, major destinations of Indian FDI outflow and inflow are Mauritius and Singapore, in Chinese FDI – Hong Kong, in Russian FDI – Cyprus and the Caribbean. Such “capital round-tripping” confirms a hypothesis that in these countries the major source of FDI inflow is of local origin.

The Russian government is trying to improve the investment climate in the country. For instance, practically each year Russia improves its position in Doing Business report issued by the World Bank. This year the country has already occupied the 35<sup>th</sup> place from the top, yet it is the last place among the Baltic rim economies (Denmark - the 3<sup>rd</sup>, Estonia – the 12<sup>th</sup>, Poland - the 27<sup>th</sup>). Radically decreased in the last years Russian FDI outflow (USD 86.5 bln in 2013, USD 38.6 bln in 2017) remains “offshore oriented” as before. ■

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MARIA ZOTOVA &amp; ALEXANDER SEBENTSOV

# New challenges to the cross-border cooperation in the Kaliningrad region

Expert article • 2417

**T**he change of geopolitical situation and mutual sanctions of the Russian Federation and the West had exerted a significant impact on the position of the Kaliningrad region, created new challenges for regional development, and warranted a revision of the old ones. A new crisis in Russia — EU relations in 2014 revitalized old discussions on the strategic development of the region as “military outpost” or the “laboratory of collaboration”.

Despite the alienating the West benefitting from the neighborhood position still may be a way to compensate the region's exclave. The analysis of implemented projects in the sphere of cross-border cooperation demonstrates that the Kaliningrad region has made good progress during the last ten years, as far as the deepening of interaction with neighboring countries (first of all, Poland) is concerned. An institutional model of cross-border cooperation was gradually constructed which led to the formation of real partnership networks, both cross sectoral ones and those concerning individual branches (environment protection, tourism, etc.). It is quite clear that there is continuity in partnership relations because any new programme demonstrates reproduction of the already established contact groups. Common interests of their participants provide prerequisite for further cooperation even under conditions of geopolitical tension.

A key distinction of the new programme period (2014—2020) is a transition from a trilateral cooperation format to a bilateral one. As in the previous years, among priorities proposed by the European Commission, the programme participants can choose and adopt those of them, which meet their interest the most. By the beginning of 2018, financial agreements between Russia and the European Union as well as framework documents concerning the Cross-border Cooperation (CBC) Programmes “Poland-Russia 2014—2020” and “Lithuania-Russia 2014—2020” have already been signed, and a joint monitoring committee has started its work. A package of requests for large-scale projects with obligatory infrastructural components is being formed. These projects include “From Spit to Spit” bikeway, the construction of a waste treatment facilities in Yantarny and Rybachy, the construction of a beach promenade, a park and marina in Svetly, improving water supply and waste water treatment, the construction of a road in Gusev, and some others. It is known that the total allocated budget of the Poland-Russia crossborder cooperation Programme will run to 62,3 million euros (including 20,6 million euros from funds of the Russian Federation) while that of the Lithuania-Russia Programme will exceed 23,5 million euros (including 7,8 million euros contributed by Russia). The first call for Proposals for both Programmes has already passed. Altogether 175 project proposals have been submitted to the Joint Technical Secretariat (118 Proposals — for the Poland-Russia CBC Programme and 57 project proposals for the Lithuania-Russia CBC Programme). The largest number of applicants are interested in

implementing projects for promotion and preservation of the natural and cultural heritage of the Polish-Russian borderline.

Interviews with Russian and Polish experts, performed in 2012, 2014, and 2017, testify that local and regional actors of cross-border cooperation demonstrate relatively low sensitivity to hostile rhetoric on both sides of the border. The transition to a real militarization of common border areas, however, could lead to a loss of accumulated experience of cooperation, as it already happened with the Local Border Traffic.

It is known that cross-border cooperation as one of the most depoliticized forms of international relations fosters the growth of confidence and facilitates the improvement of relations on a state-by-state basis. By establishing close contacts between people, it will be easier for the region to integrate itself into all-European space and to overcome negative consequences both of its political isolation from the West and its isolation from mainland Russia. Despite all complexities of negotiations, the tense international situation had no impact on the funding and implementation of cross-border cooperation projects in 2014—2018. Regional level officials on both sides of the border hope that the recently launched ENPI cross-border cooperation programmes will not suffer from mutual sanctions exchange; they consider these programmes to be “the last frontier” of cooperation. ■

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HELI SIMOLA

# Finnish-Russian trade recovering gradually

Expert article • 2418

**F**inland's trade with Russia has largely followed the general trends in Russia's foreign trade in past years. Similar to Russia's overall foreign trade, Finnish-Russian trade is largely based on traditional comparative advantage. Russia exports commodities, mainly oil and gas, and imports more sophisticated investment and consumer goods. Therefore a key factor that shapes Russia's foreign trade development is oil price. Other factors affecting Russia's foreign trade in past years have been China's rise in the global economy, increasing protectionism and recently geopolitical tensions including economic sanctions. They have also shaped the trends in Finnish-Russian trade.

The value of Finnish exports of goods and services to Russia reached its previous peak of 7.8 billion euros in 2012. Exports began to contract in 2013, as Russia's economic growth slowed down due to structural problems of the economy. When the average Urals oil price plummeted nearly 60 % in 2014–16 and the ruble depreciated by over 40 % against the euro, Finnish exports to Russia lost about half of their value hitting a low of 3.9 billion euros in 2016. Last year exports turned to brisk growth of nearly 20 % as Russian economy started to recover and the ruble regained its value. This year export growth has lost steam and even stagnated lately due to sluggish recovery of Russian demand and renewed ruble depreciation.

Finland has lost market share in Russia slightly in recent years. This partly reflects the general competitiveness problems that have hampered Finnish exports, but also e.g. the spectacular rise of China. Due to its strong competitiveness and integration into international value chains China has gained market shares both globally and in Russia. China's share in Russian imports has more than doubled during the past decade reaching over 20 % in 2017.

The mutual economic sanctions by several western countries and Russia after Russia's illegal annexation of the Crimean Peninsula in 2014 have had a negative effect on Russian trade and Finnish exports to Russia. It is difficult to separate the effect of the sanctions, but the available evidence suggests that it has been smaller than that of other factors<sup>1</sup>. The direct effect from the EU sanctions on Finnish exports to Russia is moderate, as the sanctions concern only a narrow selection of items that Finland has not exported much to Russia (even before the sanctions they accounted for only about 30 million euros or 0.5 % of Finnish exports to Russia<sup>2</sup>).

The impact of Russia's sanctions has also been limited in the aggregate level, but for individual products and companies effects have been more severe. Russia's import bans on several foodstuffs have practically ceased exports of these products from Finland to Russia. Their value was about 280 million euros or 4 % of Finnish exports to Russia in 2013. Although Russian sanctions were initially linked to the western sanctions, they are not anymore. Indeed they seem to fit well Russia's general policies of protectionism, import substitution and self-sufficiency. These trends are not new or unique for Russia, but they have been reinforced substantially after heightening of tensions between Russia and the West.

Trends in the value of Finnish imports of goods and services from Russia are largely defined by oil price, as oil and gas account for the majority of imports. Last time the imports peaked in 2011 at 11.3 billion euros, but lost over half of their value during next years. They started to improve slightly already in 2016, but the recovery gained pace only last year to 18 % with the import value totaling 7.3 billion euros. Import growth was supported mainly by higher oil prices, but received also a boost from one-off gas pipe deliveries apparently to be used later for the construction of Nord Stream 2 pipeline. This year, growth has moderated e.g. due to the base effect from the pipeline deliveries.

Russia continues to be an important trading partner for Finland, although its significance has declined during the latest years. Currently Russia's share is about 5 % in Finnish exports and nearly 10 % in Finnish imports of goods and services. Finnish-Russian trade is expected to continue growing this year, but only moderately due to Russia's sluggish and uneven economic recovery. In longer term, there is also potential for increasing Finnish-Russian trade, but currently it is restricted by Russia's relatively modest growth perspectives, increased protectionism and geopolitical tensions. ■

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<sup>1</sup> Korhonen & al. (2018). Sanctions, counter-sanctions and Russia. Effects on economy, trade and finance. BOFIT Policy Brief 4/2018.

<sup>2</sup> Berg-Andersson & Kotilainen (2016). Pakotteiden vaikutus Suomen vientiin Venäjälle. ETLA Muistio 45.

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# Cross-border tourist routes in the Finnish-Russian borderland

Expert article • 2419

Nowadays cross-border tourist routes are considered as a factor for the conservation, reproduction and the promotion of natural, historical and cultural potential in the borderland. The development of cross-border tourist routes is the step for raising the attractiveness and for boost business activities on the both sides of the border.

The unique natural, cultural and historical heritage as well as economic and institutional conditions are a base for designing and developing cross-border tourist routes in the Finnish-Russian borderland. Cross-border tourist routes development in the Finnish-Russian borderland has some features in comparison with similar kind of routes in EU-borderland. At first the configuration of the routes is pre-determined by border checkpoints. Custom and border-crossing formalities as well as the capacity of tourist companies along the route have a significant meaning for cross-border tourism development.

The European Neighborhood and Partnership Instrument cross-border cooperation programs (2007-2013) is one of the most effective tools for the implementation of international projects aiming to design and development of cross-border tourist routes between Finland and Russia.

Some of cross-border tourist routes in Finnish-Russian borderland reproduce trade and other historical routes that existed in the past between adjacent countries. The "King's Road" tourist route is for instance of historical royal road (the 13<sup>th</sup>-16<sup>th</sup> centuries) connecting modern Sweden, Finland and Russia (Leningrad region, Russia). Another example is "White Road" tourist route reproducing of the ancient trade route from the White Sea to Baltic (modern Northern Finland — northern districts of the Republic of Karelia, Russia). An important of the project was the opening of six tourist information centers in the several districts of the Republic of Karelia.

"Blue Road" tourist route (ca. 2000 km) is a successful project of cooperation and tourism development that runs from Norwegian town of Nesna through Sweden and Finland to Russia (the Republic of Karelia). The development of the "Blue Road" tourist route is of fulfilling the sustainability requirement by an international project. The "Mining Road" tourist route (ca. 400 km) elaborated within international project unites about 20 main objects associated with the geological, mining and industrial heritage of the Finnish-Russian borderland (North Karelia, Finland — the Republic of Karelia, Russia). One of the main outputs of the KA 334 "Mining Road" project in Russian part

is a creation of a new tourist attraction — Tulmozero Ore Park from mining plant ruins (XIX-XX centuries). Now Tulmozero Ore Park is one of a perspective tourist site where according forecast the number of visitors achieve 20-30 thousand peoples per year. Also in the framework of project was produced a set of audio-guides facilitating unaccompanied visits to attractions along the route. Another example of the involving geological potential of the northern Fennoscandia in the tourism is the circular Barents tour uniting Norway, Finland and Russia (Murmansk region, Kola Peninsula).

The designing cross-border gastronomic tour will be elaborated within international project "Kalitka — the development of cross-border gastronomic tourism" (approved by the European Neighborhood Instrument cross-border cooperation programs). It will be an route of gastro-tourism development in Karelia region (North Karelia, Finland — the Republic of Karelia, Russia).

Cross-border tourist routes development is one of success tool for developing cooperation between border regions of Finland and Russia. These routes can be considered as a tool for exposing the potential of the Finnish-Russian borderland and drawing it into economic circulation. Such routes form the basis for diversifying the tourist product and for the implementation of local initiatives.

One of the key results of the designing and developing cross-border tourist routes are infrastructure development, invigoration of the business activities on the both sides of the border as well as an increase in the number of visitors at sights and facilities along the routes. Along with large opportunities for cross-border tourist routes development some hindrances in the Finnish-Russian borderland exist. Designing and developing cross-border tourist routes can be considered as a step towards a transboundary tourist space. ■

Cross-border tourist routes development is one of success tool for developing cooperation between border regions of Finland and Russia.

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ADAM A. AMBROZIAK

# Russia's embargo on the Polish apple exports

Expert article • 2420

In recent years we observe an escalation of trade barriers introduced by countries for some complex reasons. From economic and legal points of view, restrictions in international trade are used to protect domestic market against foreign (sometimes unfair) competition, to force a given country (or a company) to stop unwanted actions, to change its behaviour (internal or external), as well as, to eliminate negative consequences of previous activities. From political point of view, sometimes they can be interpreted as a reaction of international society against a country which is in breach of law or any agreements. Therefore, one can state that political sanctions, in contradiction to economic-based measures in trade (e.g. antidumping or anti subsidy duties), are being introduced purely as a consequence of political decisions often made on the basis of current political developments without reflecting on future economic consequences.

In the era of a rapid growth of international trade, digitalisation and servitization of manufacturing, and strengthening of the global value chain, it is worth underlining that the aforementioned instruments applied against the exchange of goods affect not only the country, against which they are introduced, but also domestic economy, which is cut off from imports. At this same time, the presence of many international economic organisations and trade preferential agreements which, bilaterally and multilaterally, liberalise trade among the contracting countries have a spectacular impact on sanctions' effectiveness.

The aforementioned thesis can be confirmed by the analysis of consequences of two Russia's embargos on imports of selected goods from Poland. These measures were put in place to different extent, under different circumstances and for two different reasons. In 2005, only 18 months after Poland's accession to the European Union (EU), the Russian Federation launched the first embargo on exports of Polish agri-food products, including apples. The main argument raised by Russian authorities concerned the compliance with phytosanitary requirements, the restrictiveness of which unexpectedly substantially increased, while border control was enhanced. It should be noted that Poland, a Member State of the EU, had to meet all the EU requirements. One could expect that embargo introduced by Russia, the biggest importer of apples from Poland, should negatively affect economic position of Polish farmers. It did not happen. Firstly, Polish distributors had to find new channels to export apples to Russia. The market was very important to them due to the already established linkages with Russian importers and consumer preferences and expectations (concerning price and apple varieties). Therefore, based on the free movement of goods within the EU, Poland increased its exports of apples to Lithuania, as well as to Slovakia and Estonia, which reexported them to Russia. Similar mechanism worked between Poland and two non-EU countries: Belarus and Ukraine. Finally, although Polish exports of apples to Russia formally did not exist, Polish apples were present in the Russian market. Secondly, Poland, as a member of the EU, increased its exports to other EU countries, which improved its position in the Internal Market.

Slightly different situation occurred in 2015, when Russia introduced the second embargo as a countermeasure to sanctions put

in place by the EU and the USA after a Russian invasion of Ukraine. While the first embargo targeted Poland only, the second one covered all the EU countries. Thus Polish farmers could not sell their agri-foods, including apples, through other Member States to Russia. Moreover, more restrictive customs controls at the Russia's external border and more problematic political situation in neighbouring countries resulted in the reduction in exports through Belarus, Ukraine and Kazakhstan. Therefore Polish entrepreneurs were strongly pushed to change both: the direction of exports, as well as, the range of varieties and quality of products offered to new markets. Consequently, Poland has been enhancing its position within the EU, as any agri-food product, including apples, is allowed to be sold in Poland, it can be offered freely without any discrimination within the EU. Moreover, Poland has been seeking new markets (in Asia, Africa), which is a time consuming and costly road towards export independence (from Russia).

In conclusion, we can state that a stable, liberal trade regime can assist countries in overcoming barriers introduced by their counterparts for purely political reasons. Taking trade in apples between Poland and Russia as an example, we can formulate some general observations. Thanks to the EU membership, free movement of goods within the EU Internal Market, positive and open relations with its neighbouring countries, a very wide and complex net of trade preferential agreements (based on fair and free trade principle) concluded by the EU with third countries, Poland could adjust to new economic situations (created by earlier political interventions). Firstly, farmers diversified their production to meet new customers' requirements and expectations (sometimes ensuring higher quality or new varieties). Secondly, exporters had to find new destinations for deliveries and secure that their products meet new markets' phytosanitary (technical) restrictions. Consequently, we can expect more stable export market for domestic producers and more independence of entrepreneurs from trade instruments based on political choices (especially in Russia). However, it should be underlined, that the aforementioned mechanism can work only if a given country has got an unlimited access to a big, rich market (like the EU) and is deeply integrated in free and fair international trade. So far, it seems that Poland's membership in the EU can guarantee that above mentioned economic mechanism can counteract measures applied by third countries against Polish economy. ■



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MERIT TATAR

# Developing smart and sustainable urban transport systems

Expert article • 2421

Many cities and regions in Europe and also in the Baltics are making remarkable efforts to progress towards a more sustainable and smart urban transport system. Cities need to respond to the present mobility needs without compromising the ability of future generations to meet their needs. Urban transportation systems need to evolve together with the cities and people's need to move around the city. At the same time, cities have to respond to climate challenges, especially when it comes to reducing carbon emissions. Here, urban transportation inevitably belongs to one of the most prominent challenges with no single solution or ideal model. However, technology is one common thread the cities strive for in responding to the urban mobility challenge. Technology is a basis of what constitutes the development of smart cities all over the world, a very popular and yet still entirely undefined concept. The European Commission also funds large initiatives where the energy, transport and ICT industries are invited to work together with cities to combine their technologies and address the needs of urban regions. Therefore, many cities know that there is an opportunity related to smart cities, but at the same time, many are not sure what it really means for them. What is becoming more common is the understanding that technology alone does not make a city smart, but it is the people using that technology. Technology itself is broadly neutral, it is the technology in practice that has political, social, economic and environmental effects as is also highlighted by the 'Delivering the Smart City 2017' report. Everything starts from and ends with people also in building up a smart urban transport system – it has to consider the complexity of human behavior.

Urban transport that is almost emission free but responds to people's needs is one important pillar in an ideal smart and sustainable city. Offering an alternative combination of various transport modes is a way for cities to achieve a more sustainable, environmentally friendly commuting system. However, switching from cars to alternative means of transport will only happen if alternative services respond to people's demands. A smart and sustainable urban transport system requires that various features of the whole system are strengthened, including accessibility and mobility, reliability and efficiency, as well as safety and security, social equity, convenience and comfort, as noted by many experts. The challenge is huge – transport systems should be people- and environmentally friendly, requiring changes in transport strategies, transport planning, transport investments and, most notably, in each person's transport behavior.

The European Commission is one of the biggest public funder of smart initiatives also in the transport sector for most of the cities in the Baltics. Besides several work programmes under Horizon 2020 and the rest (altogether 41 funds), there are also specific regional cooperation Interreg programmes, which have already helped to initiate valuable projects that deal with several urban transport aspects in the region. Since 2007, a total of 19 transport projects, each dedicating on average 2-3 MEUR to the issue at hand, have

been funded in the Baltic Sea Region, out of which several exclusively deal with urban mobility and include almost all the Baltic Sea Region states as partners. For example, the MAMBA project aims to improve the integration of existing mobility structures with innovative transport solutions, such as mobility as a service (MaaS), transport on demand and ride sharing applications to overcome difficulties in rural transport. Sohjoa Baltic brings autonomous small buses to drive demo routes in six Baltic Sea Region cities. BSR Electric enhances the use of electric vehicles in city transport systems such as public sector fleets, public transport and bike sharing in order to reduce CO2 emissions and pollution. The SUMBA project works towards a more sustainable and environmentally friendly commuting system, combining various transport modes such as public transport, car sharing, walking and cycling. The project helps urban and transport planners assess, plan, and integrate alternative mobility options into transport plans and policies of cities and municipalities. Cities.multimodal combines walking, cycling, public transport and car-sharing as an environmentally friendly alternative to driving. It includes publicly visible mobility points and smartphone-based travel planning among other piloted tools for the city planners and also for the citizens. There is a good cooperation initiative between Tallinn, Tartu and Helsinki dealing with e-ticketing and connecting ticketing systems to enable seamless travelling between the cities and finding ways to commute between Helsinki and Tallinn (FinEst Link and FinEst Smart Mobility projects).

The EU Smart Cities and Communities programme has funded 15 large-scale integrated smart city projects in Europe. These "lighthouse" projects, now involving 36 lighthouse and 42 follower cities all over Europe, test and implement a range of innovative solutions in specific city districts with the aim of stimulating uptake and growth in the market and the transition to a more sustainable Europe. The goal is to facilitate a successful transformation towards intelligent, user-driven and demand-oriented city infrastructures and services. These cities are focusing on measures like eliminating diesel buses from public transport, installing new electric car charging points in cities, implementing public e-bike sharing systems, developing car sharing systems, remodeling transport lines based on new ways of gathering and analyzing data, for example based on real time mobile data, advancing 3D simulation etc. Another big trend the cities are turning their attention to is mobility as a service (MaaS). This kind of development changes the way city dwellers get around. The whole idea is to make it unnecessary for any city resident to own a private car, an ambition adopted for example by Helsinki, the capital of Finland, by 2025. The dream which once would have seemed impossible is not so unrealistic anymore due to rapid advancements in technologies and system thinking that cities can use in modernizing their transport systems. Also, autonomous vehicles will play a significant role in making zero emissions transportation a reality and are already increasingly in the focus of various innovation projects. Besides that,

cities have to engage the users of the system into the planning and development phases as co-creation is the magic component of the success recipe of innovations. This, in turn, requires completely new skills from city administrations and politicians in ways to plan ahead and engage people. As important as are physical conditions for public transport (convenient vehicles, waiting areas, different modes to choose in between), people need accurate real time information and user-friendly applications for travel planning. Cities search for the best solutions to make functionalities like travel planning, real time travel information, navigation, maps, personalization, payments, data analytics etc. all as convenient and important parts of such systems and a decent variety of solutions already exists in this area.

These are some of the examples where the Baltic cities are also involved. Inevitably, there are several barriers that cities face while transitioning their energy and transport systems, whether they are legal, technical, economic, social. Finding proper funding is always an issue, but while working with and talking to city officials in these projects, one can discover the key to these transitions – this is the attitude and openness to future innovations and cooperation. Smart cities need an integrated approach, strong willingness to think differently and out of the box. The deputy mayor of Tartu, the only Lighthouse city in the EU Smart Cities and Communities programme from the Baltic States, Mr Raimond Tamm, has said that making a city smart is like putting together a puzzle - you never know how the puzzle should be assembled piece by piece so the bigger picture would finally take shape, this is a puzzle that will never be completed as it is always getting bigger, but putting it together with knowledgeable and open-minded partners and citizens enables to get there quicker.

There is an overwhelming agreement in Europe that cities should do more to exploit the solutions developed within different projects and benefit from already available know-how. There is a lot of that already! Even though cities face their own unique challenges and will find unique solutions for the people who live and work there, all race towards the same goal of reducing emissions.

The Thinking Cities magazine has recently published a very good overview of thoughts and cases about smart transport for cities and regions. Several authors in the issue have highlighted that in order to see through the changes that are being implemented, to ensure they are not here-today, gone-tomorrow flashes of brilliance that are not founded on the needs of the city or its citizens, we must build on existing knowledge, develop transferability tools, share practices across borders to ensure that European cohesion at the local level becomes a reality. Commonalities and key learnings to be shared will only accelerate advances towards cleaner, more connected and increasingly sustainable transportation systems. Change needs to be embraced, and not shied away from it. It is true in all smart city developments and not just in innovating urban transport systems that sometimes in order to achieve results you just need to change the angle of thinking. This is something that everyone should keep in mind, whether in the role of decision makers and specialists in the city or citizens using the services. ■

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# Developing a regulatory framework for autonomous shipping

Expert article • 2422

**T**he exponential progress in technology is pushing the world inexorably towards the dawn of autonomous shipping. Advances in broadband capacity, big data, high-speed processing, and rapid interconnectivity are enabling more shipboard automated systems to be remotely controlled. Research and development will presumably continue at an uninterrupted pace until the unmanned ship finally becomes a commercial reality. Proponents of the development of maritime autonomous surface ships or "MASS" submit that such ships hold great potential for even safer seas, cleaner oceans, and more efficient shipping.

Automated systems will enable ships to more efficiently react to weather disturbances and compensate for wind and currents – leading to fuel savings and less pollution. They will minimize or eliminate the need for humans to be present for some of the most hazardous and labour-intensive aspects of ship operations such as the monitoring or securing of cargo and dealing with engine or machine failure. The reduced reliance on human labour will make preventive and predictive maintenance more regular and routine. The possibilities for optimizing efficiencies are endless.

As technology companies team up with their maritime counterparts, so has the shipping sector rapidly begun to realize that some of the most difficult challenges it faces are understanding the nature of this disruptive technology and the effects of its integration within existing shipping infrastructures, operations, and processes. The development of maritime autonomous technologies need to be guided by a regulatory framework that will ensure such applications will only serve to enhance the interest of the greater safety of life, property, and the environment. To be sure, a myriad other issues need to be answered such as security, pollution, liability, compensation, ethics, education, training, testing, data transfer, cybersecurity, systems architecture, communications, connectivity, reporting, artificial intelligence, etc.

Keeping the law abreast and in pace with science and technology has always been a challenge throughout history, and the advances in autonomous transport technology is no exception. The International Maritime Organization (IMO), being the United Nations specialized agency responsible for the safety and security of shipping and the prevention of pollution by ships, has decided to address this issue squarely and proactively and take the first important steps in a long and comprehensive process towards developing a solid international regulatory framework for MASS. At its 99<sup>th</sup> session last 16-25 May 2018, IMO's senior technical body – the Maritime Safety Committee (MSC) – commenced work to determine how MASS operations may be addressed in international maritime agreements and instruments.

The May 2018 MSC meeting agreed on a way forward for conducting a regulatory scoping exercise. The work included preliminary definitions of MASS and degrees of autonomy, as well

as a methodology for conducting the exercise and a plan of work. As a preliminary definition, MASS was described as a "ship capable of operating independently of human actors to varying degrees." The degrees of autonomy are as follows:

- Ship with automated processes and decision support: Seafarers are on board to operate and control shipboard systems and functions. Some operations may be automated.
- Remotely controlled ship with seafarers on board: The ship is controlled and operated from another location, but seafarers are on board.
- Remotely controlled ship without seafarers on board: The ship is controlled and operated from another location. There are no seafarers on board.
- Fully autonomous ship: The operating system of the ship is able to make decisions and determine actions by itself.

It was noted that MASS could operate at one or more degrees over the course of a single voyage. The scoping exercise will survey relevant IMO instruments for existing provisions that may relate to or affect MASS in one way or another. Subsequently, the exercise will analyse and determine the most effective ways to address autonomous ship operations. The MSC has called on the member states of IMO as well as other international organizations to submit proposals for the development of interim guidelines for MASS trials ahead of the 100th session of MSC in early December 2018.

It might be argued that we are not as yet on the cusp of unmanned and autonomous shipping, but that we are certainly moving in that direction. In the meantime, the absence of universal standards governing the development of relevant technologies could never be in the best interest of the maritime public. The challenge facing the maritime sector today is to ensure that the IMO's membership is fully informed and that the international regulatory framework stays abreast, or at least does not lag too far behind, technological developments in autonomous shipping. ■



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# Global challenges call for local response through common goals

Expert article • 2423

The past summer broke temperature records across the world, and subsequently evoked a heated discussion in the global media over climate change. Extreme weather phenomena across the planet have now concretely brought the issue to the surface, despite the fact that the first scientists called action over the matter as far back as the 70's. It is also already more than decade since the acclaimed Stern report, in which the economist Howard Stern showed that the externalities of climate change would eventually cost more to the global economy than if actions to slow it down were taken immediately. 12 years later, and we have finally begun to recognise the fact that "business as usual" cannot exist any longer. In our aid we have several recommendations, guidelines and goals set by international bodies; the most distinguished of which perhaps being the Sustainable Development Goals (SDGs) launched in 2015 by the United Nations' Framework Convention on Climate Change.

This set of 17 goals represents a global intention to create a more sustainable, or even re-generative future for the coming generations. These SDGs succeed the Millennium Goals (MGs), active between 2000 and 2014, but differ from their predecessors most prominently on their target audience; while the MGs were aimed at the developing countries, the SDGs have been set for the whole world. Additionally, the SDGs are equipped with targets and indicators, which are intended to ease the work for the individual national monitoring committees. The SDGs cover the whole spectrum of life on the planet, societies and culture, the flora and the fauna, above and below the sea level. They are by no means called 'ambitious' without reason.

The American cultural anthropologist Margaret Mead has famously stated that one should *"never doubt that a small group of thoughtful, committed citizens can change the world; indeed, it's the only thing that ever has."* Regardless of the many good-will gestures of governments committing to the famous Paris Agreement during COP21, it can be argued that the actual implementation of the SDGs relies on the work of smaller, dedicated, professional groups – such as projects with their professional consortiums to integrate the Goals in their companies' policies, visions and missions, across their business agenda. One such group is currently working around the Baltic Sea region; the project consortium of ECOPRODIGI has now been in action for a year, developing digital, more eco-efficient processes for maritime industry.

The project consortium consists of 21 partners across the Baltic Sea, including research institutes such as the Lead Partner Pan-European Institute at the University of Turku and Chalmers University of Technology in Sweden; industrial partners Meyer Turku and Western Baltic Engineering shipyard in Klaipeda, Lithuania; and business consulting firms including OSK-ShipTech from Denmark and

Carinafour from Finland. The resourceful project was recently been granted a Flagship status by the European Union Strategy for the Baltic Sea Region (EUSBSR), implying that the project is aligned with the Strategy, namely with its objectives to 'Save the Sea', 'Connect the Region' and 'Increase Prosperity in the Region'.

EUSBSR and its objectives were set in 2009, and the Strategy acts as the first Macro-regional Strategy in Europe. It strives to strengthen cooperation between the Baltic Sea nations in order to deal with their mutual challenges and find common ground to connect. It is implemented through projects and processes which are recognised to support and demonstrate its objectives. One does not have to look far to appreciate the alignments between the EUSBSR's objectives and the SDGs: both seek to strengthen global cooperation in order to provide a better standard of living to its citizens, and ensure that the environment is being protected in the process.

Why are objectives and goals such as the SDGs, and the EUSBSR's objectives so important? Because they give projects and initiatives relevance at a global scale; e.g. ECOPRODIGI is directly contributing to SDG #14 "Life below water" to name but one, by aiming to reduce emissions in the sea and water through eco-efficient solutions for the whole vessel life-cycle. The ultimate goal is to develop solutions which can then be applied to every sea in the world, not just the Baltic Sea. By connecting the work to EUSBSR's objectives, the project gains macro-regional support; and connecting the work to the SDGs, the project is responding to common global challenges at a local scale. Indeed ECOPRODIGI has recently joined a project platform 'CSHIPP' with six other projects acting under the 'Clean Shipping' agenda, joining their forces with a mission to support each other and share the results and best practices derived from each project further. By aiming to achieve common goals, ECOPRODIGI and the fellow projects are leading the way to make the Baltic Sea region a model region for clean shipping and sustainable development for maritime industry in the world. ■



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# Shipbuilding – reality and challenges for Poland

Expert article • 2424

**T**he shipbuilding industry has always been a global industry influenced by global economic trends, which can be seen in particular in tonnage prices and costs of steel and a huge impact of exchange rates on this industry.

According to the EU policies, the member states or regions are allowed to receive financial aid from the Community. In Poland, however, awareness of the EU's actions and initiatives focused on the shipbuilding industry has always been insufficient, sometimes leading to various misinterpretations. One of the consequences was a passive approach of our representatives negotiating Poland's accession to the European Union, which resulted in hardly any (practically: none) provisions concerning the shipbuilding industry in the Accession Treaty.

The relevance of this problem was recognized by the European Union, which commissioned the LeaderSHIP 2015 report whose aim was to answer the following question: how can key challenges faced by the European shipyards be solved? The former European Commissioner for entrepreneurship, E. Liikanen had once said: "European shipyards and their suppliers are truly high-tech undertakings, constantly introducing new products and technologies. Our yards have what it takes to succeed in the global market. They have reinvented themselves time and again in the face of adversity. But for a successful future this must be complemented with decisive political support, based on appropriate policy targets and a longer term vision"<sup>1</sup>.

The shipbuilding industry is seen by the EU member states as part of the economy whose output is highly processed, and the final product is a driver of high-tech solutions. The shipbuilding industry is recognised as a sector of the economy which contributes significantly to the growth of other industries.

Shipyards can successfully become a "growth pole" in the national economy, creating an export promoting zone, thus accelerating growth in their immediate environment and improving the region's competitive advantage. Furthermore, economic growth of the shipyard and its environment generates new jobs for the existing and predicted labour force not only in a given region but also in other regions where strategic co-operators in the shipbuilding industry are based.

Well targeted subsidies from the budget, i.e. state aid targeted at a shipyard, can be a factor determining the yard's survival and potential to compete in constructing the most advanced and hi-tech ships. When analysing the prices of the ships offered by South Korean or Chinese shipyards, there is no financial justification for their level from the viewpoint of the European economic reality.

The prices which are contracted (not the offered ones), and which are approx. 20 per cent lower than the prices offered by the shipyards in Europe, should be hence recognized as dumping. When analysing

the manufacturing conditions in the Far East, no economic or technological evidence can be found to prove that shipbuilding at these levels of final prices is actually financially profitable.

Nevertheless, financial unprofitability does not equal economic unprofitability. The role of shipyards as growth poles, innovation centres or export promoting centres reveals how they are different from many other companies. Hence, in order to protect jobs in the shipbuilding industry in Poland and the entire European Union, it is essential to introduce a standard system of subsidies, develop a common strategy and undertake joint efforts aimed at protecting this industry. Such initiatives, however, are not met with understanding, as there are major differences in interests between individual countries.

There are two distinct trends that can be observed within the global shipbuilding industry. The shipbuilding industry in the Far East is an element of huge centralised economic structures. Although there are certain differences between the Japanese concerns and the Korean chaebols, both are usually huge conglomerates with shipyards operating only as their parts. The shipbuilding industry in China seems to be developing following a similar path.

The European industry, on the other hand, is highly dispersed, which can be attributed to the continent's history. Still, even here consolidation efforts can be observed, particularly in Germany and Finland, where first attempts of creating shipbuilding holding companies or concerns with diversified production are made (e.g. Thyssen/Krupp, Alstom). Next to the consolidation of capital, which implies centralised management, other forms of consolidation can also be observed, e.g. integrating, partnerships between individual shipyards or their development, logistics and marketing departments. The Dutch organisation CONOSHIP is a good example of such a structure; it groups activities of shipyards in two regions – Friesland and Groningen.

When discussing the major challenges faced by the shipyards operating in Poland, the following questions need to be answered:

1. Are shipbuilding yards business entities which structurally generate losses on business activity?
2. Will the support (subsidies) translate into higher revenues to the budget exceeding the outflows? In other words, will the end result of the budget-shipyard game be a positive or negative one?
3. Are shipyards important to the regions they operate in and to the national economy?
4. Is consolidation of shipbuilding yards and ship repair yards a good solution?

An unambiguous answer to the question whether shipyards generate losses or profits should be backed by estimation of the shipyard's Break-Even Point, yet there are too many factors which determine this level. Furthermore, high volatility of individual cost items (such as frequently abnormal levels of global steel prices) requires extreme caution when solving this problem.

<sup>1</sup> LeaderSHIP 2015 A Road Map for the Future of the European Shipbuilding and Ship – Repair Industry.

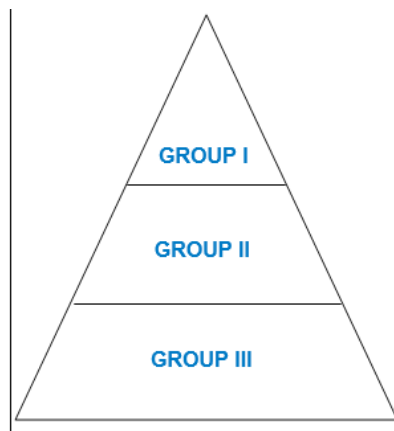


Periods of prosperity enjoyed by our shipyards can be easily identified. They were usually related to the boom in the freight transport market which drove the prices of ships up. Ex-change rates and commodity prices were also in favour of this industry's development. It should be emphasised that it is Polish zloty, Euro and the US dollar exchange rates that contribute the most to a shipyard's profit from operations. The global currency game is a factor which remains entirely beyond any shipyard's control.

When addressing the second issue, i.e. the tax game between the budget as an institution providing state aid to the shipyard, it can be easily shown that the final result of this game is a positive one from the viewpoint of the budget. It means that the government, using subsidies, is able to stimulate the shipyard's operations and receive in return huge amounts of taxes not only from the shipyards alone but also from other entities forming the complex chain of suppliers and co-operators.

We can frequently come across a statement that the "old" EU member states are able to subsidise their industry because they are rich. In fact, nothing could be further from the truth. There is no country in the entire world that would be rich enough to subsidise a broad spectrum of the economy, as it is taking place in Europe. EU member states do provide subsidies to a wide array of industries for social reasons but also because their aid strategies lead to a positive or – in the worst case – neutral final result to the budget.

Figure 1. Classification of companies



a. **Group I** are entities which sell their products or services outside the region, i.e. some-where else in the country and abroad. Group I companies determine economic growth of the region or country because they "export" outside their immediate area thus bringing money to the region. These companies and their employees generate also increasing demand for the goods and services sold within their area of activity.

b. **Group II** are companies which (with certain degree of simplification) deliver their products or services directly to Group I. This group comprises suppliers of energy, as well as providers of construction, transport and financial services etc.

c. Finally, **Group III** is comprised by companies delivering widely available goods and services, such as shops, local banks, restaurants, craft businesses, petrol stations and other companies identified as small and medium-sized enterprises.

As for the fourth issue, i.e. consolidation of assets and finances of shipbuilding and ship repair yards, the answer is also ambiguous. It is a much more favourable situation if the ship-yards (regardless of their profile of activity) operate within a larger economic structure, yet each case should be approached and assessed individually.

Well targeted state aid for a shipyard can not only drive growth of the shipyard alone but – as mentioned above – it can also stimulate development of a growth pole around it.

In 2008, when detailed estimates were made in this area, it was reported that the total sub-sidy planned for the Szczecin Shipyard would not exceed **PLN 70 million**, while the net balance of public-private revenues (after subtracting the subsidy) would reach nearly **PLN 122 million**. The aid applied for must, naturally, meet the EU's state aid requirements, yet in this case it is evident.

#### FINAL REMARKS

An analysis of the process of changes and transformation of the shipbuilding industry was carried out by a team representing the Association of Polish Maritime Industries FORUM OKRĘTOWE<sup>2</sup> and shown in the "Strategy for the Polish Shipbuilding Industry". A thorough study of this document allows the following conclusions to be drawn and challenges to be identified for the long-term strategy:

- so far none of the transformations were aligned with a clearly defined strategy for the industry. Such a strategy was represented by neither the government bodies nor the top-level management in the shipbuilding industry.
- except for very few cases, privatization was processes without capital, which means that companies started processes practically without any resources and with a huge debt instead,
- production overcapacity, shrinking shipbuilding industry in Europe did not attract any foreign investors,
- an example of good practice is privatization of the REMONTOWA Ship Repair Yard in Gdansk,
- debt-relieving undertakings have significantly affected co-operators, substantially de-creasing their wealth. It refers mostly to companies with high share of shipbuilding operations in their profile.

Long production cycles and high cost of shipbuilding and ship repair require engagement of substantial financial resources. Under the LeaderSHIP 2015 programme it is pointed out that in most of the countries where the shipbuilding industry they are developing positively, public (state) institutions offer financial support to shipbuilding; there are, however, many options. While the US Maritime Administration guarantees loans up to 87.5 per cent of the total contract value for 15 years, and the Korean KEXIM-Bank provides total financing packages covering loans and guarantees prior to and following the delivery up to 90 per cent of the contract value – few EU member states offer funds for this purpose. It is therefore recommended to investigate the

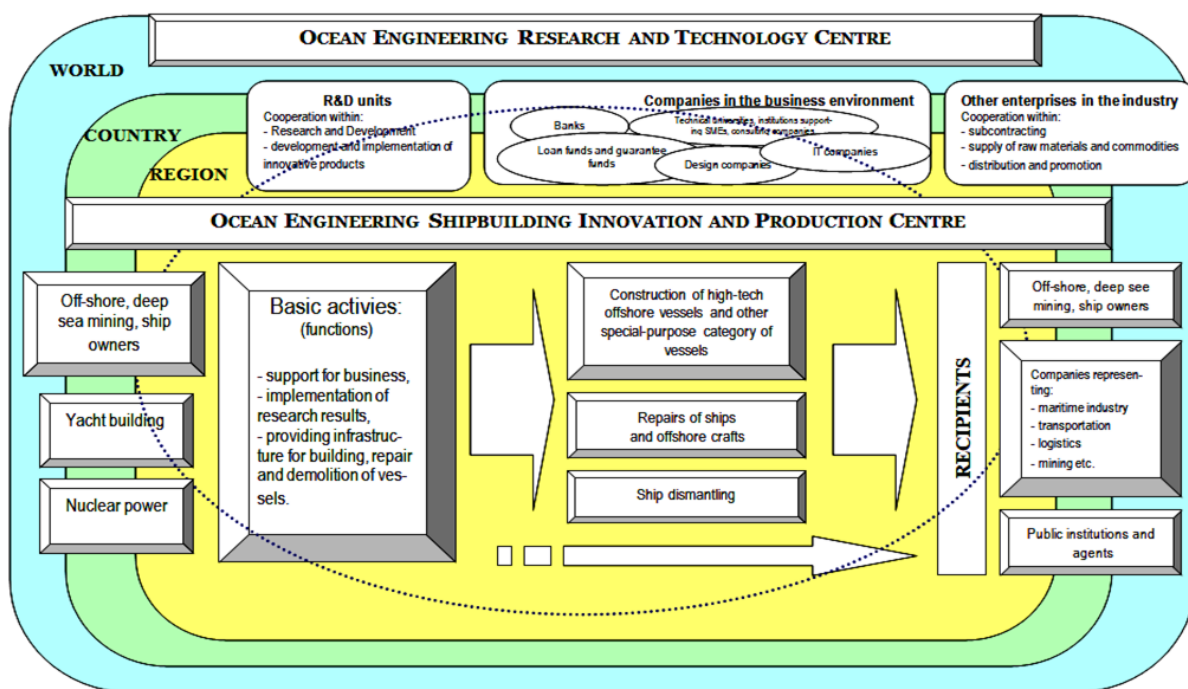
<sup>2</sup> "Strategy for the Polish Shipbuilding Industry" – by the Association of Polish Maritime Industries "Forum Okrętowe" of November 2004.

possibility of forming such a guarantee fund for the entire European Union.

Currency risk is a separate challenge which needs to be faced by Polish shipyards and their co-operators who export their goods/services. In Europe, where this factor is much less significant, several countries such as France, the United Kingdom or the Netherlands offer facilities in this area. The recent dramatic changes in the USD/PLN exchange rates require decisive protection of USD-denominated exports as the efforts of shipyards to switch to EUR-denominated contracts are mostly fruitless given the popularity of USD-denominated contracts.

At the moment, we are witnessing in Poland the formation of financial engineering mechanisms oriented at the shipbuilding industry, including the government, financing sectors, ship owners, shipyards and co-operators.

What still remains unsolved is the problem of finding an economic alternative to shipyards, i.e. establishment of a similar, in terms of scale, employer who will be able to offer well-paid and stable employment to many people. In other words, it is essential for our country to identify its position in the global division of labour – which is possibly Poland's greatest challenge for today. ■



Picture 1: Diagram of potential relationships in the maritime industry in Zachodniopomorskie Voivodship  
Source: own study based on the methodology by the Gdańsk Institute for Market Economics (IBnGR)

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# Deep sea mining – raw materials new perspective

Expert article • 2425

**D**eep ocean polymetallic nodules are considered as a potential resource for nickel Ni, copper Cu, manganese Mn and cobalt Co. Recent research showed they contain as well a large variety of other metals including molybdenum, zinc, lithium, titanium and some REEs (rare earth elements), which increased their combined value as an alternative supplies for expanding economies and emerging green technologies. Research of alternative energy shows that green technologies are more Ni and Cu intensive than conventional energy. A single wind turbine requires roughly 12 times more Cu to produce 1kW than conventional power generation; an electric car requires twice as much Cu than a conventional car. Estimates for the amount of Ni contained in NiMH batteries used in the electric vehicle was counted to increase by a factor of more than ten between 2003 and 2018.

The International Seabed Authority (ISA) granted exploration contracts (licenses) for polymetallic nodules to 17 national, multinational and commercial entities, each covering 75000km<sup>2</sup> in the international seabed area. Those seabed regions ("the Area") are beyond any national jurisdictions and are under the administration of the International Seabed Authority (ISA) in accordance with the 1982 UN Convention on the Law of the Sea (UNCLOS). The ISA is the only international institution responsible for regulating and controlling activities associated with the exploration activities in the Area. The ISA is in the process of developing regulations (Mining Code) to govern prospecting, exploration and exploitation for polymetallic nodules, including fiscal matters (mining royalties). The provisions of the contracts require contractors to carry out activities and to report to the ISA on implementation of exploration plan of work, environmental studies, the development of mining technology and other legal and financial issues.

The Interoceanmetal Joint Organization (IOM) is an intergovernmental consortium certified by the governments of Bulgaria, Cuba, Czech Republic, Poland, Russian Federation and Slovakia. IOM signed in 2001 the contract with the ISA for exploration of polymetallic nodule deposits. In the implementation of the plan of work for exploration IOM cooperating States carry out comprehensive R&D studies in geology, marine environment, mining technology and processing of polymetallic nodules as well as deep sea project business development.

Resources of nodules in the eastern equatorial Pacific within the so-called Clarion-Clipperton Fracture Zone, (CCZ) contain 1.1 times more Mn, 1.8 times more Ni, 3 times more Co. It is estimated that metals in CCZ as percentage of the total global land-based reserves are Cu 20%, Mo 60%, Li 20% and REEs 10%. Nodules contain 7.5 thousand million tonnes of Mn, 340 million tonnes of Ni, 285 million tonnes of Cu and 75 million tonnes of Co with 2.5% combined content for Ni+Cu.

Recent economic models for mining of these deposits indicate IRR of between 10% - 30% in different economic scenarios. The extraction at great depth of abt. 4500m is considered the key component in the deep sea mining commercialization and involves never before attempted technological, environmental and legal issues. The very recent trials of mining conducted in the Area by some of the ISA contractors proved the technical viability of the deep sea mining enterprises.

The interest to develop polymetallic nodules is result from growing demands for metals by the rapidly developing countries such as India, China, Brazil and continuous depletion of land deposits. Decreasing ore grade of terrestrial deposits with the resulting increase in energy requirements and quantities of waste that must be disposed also affect the potential deep-sea mineral resources. The EU countries are in the face of shortages in the supply of REE and other metals considered critical "technology metals" e.g. Ni, Co, Mn, Ge, Ti etc., are essential for the development of many branches of industry, including electronics and emerging technologies. Metal prices today are affected by factors external to the industry and they continued to be unsteady. Higher metal prices between 2005 and 2009 encouraged the exploration, planning, and development of many new Cu-Co and Ni-Co projects, including deep sea minerals. Nickel will be the mainstay of the nodule mining industry. Cu, Co and Ni will be produced jointly with manganese markets products and several trace metals as by-products from the tailings.

The deep sea mining is one of the most potentially rewarding frontiers that challenge mankind in its exploration activity for minerals to ensure sustainable development and raw materials supply. The commercial viability of nodule mining has yet to be established, but the size of deposits, the grade of several metals contained in nodules and the promising trends in metal market motivate contractors to carry out their exploration activities. ■

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# Seeing potential of young return migrants to Latvia

Expert article • 2426

**D**evelopment of migration history in Latvia has taken several turns. Latvia as one of the Baltic countries along with collapse of the Soviet Union (early 1990ies) experienced major out migration flows eastwards. After a decade (after 2004) when Latvia became member of the European Union migration direction turned westwards. Latvia thus became country of emigration with rather steady out migration flows as people used the possibility to move abroad and experience free movement of people with the EU. Following major outflow from Latvia occurred during period of insecurity and instability at the period of sharp economic decline known as the Great Recession (after 2008) when GDP dropped by 14.4% and even 18 % (in industry of financial intermediation) simultaneously with the sharp increase in unemployment rates (according to Eurostat 14.4%). The highest numbers of emigration from Latvia were in years 2009 and 2010. In year 2010 the number of registered out migrants from Latvia reached 39 651 persons. Year 2014 which correspond to the post-crisis period constitute number of emigrated persons around 19 000. Since then westward out migration remain stable. There were 17 724 registered emigrants in year in 2017. Post-crisis period can be characterised as economic recovery which is evident in GDP growth (4.5%) and increase in labour market dynamics (according to Central Statistics Bureau of Latvia unemployment rate in year 2017 was 8.7%).

The main destination countries for Latvian emigrants are the United Kingdom, Germany, Ireland, Sweden and Norway. Last five years have brought reasonable stability in terms of emigration rates of Latvian citizens as well as stable return migrant flow. Rates starting from post-crisis period show rather steady results and yearly around 5000 persons return to Latvia. Over 60% of all immigrants to Latvia in year 2017 were return migrants.

According to the recent Horizon 2020 programme project "YMOBILITY" (grant no. 649491) on youth intra-European migration patterns migration as such, circularity and return migration is individually beneficial and human capital growth obtained abroad can further be exploited at the country of origin. It was evident from the

study that young people return as they hold strong association with the home country. The study also confirms that the main gain from the migration experience is improvement in foreign language skills, acquaintance with labour market abroad as well as possibility to earn more. Individually young return migrants after the return highly value their ability to deal with new challenges they experience upon return, self-confidence and acceptance of cultural diversity.

Topicality of return migration discourse in academia, society and policy makers in Latvia have resulted in policy initiative. It is worth noticing that there is a pilot project 'Regional remigration coordinator' in Latvia enhancing regional return migration. Project is coordinated by the Ministry of Environmental Protection and Regional Development. Practical work of five regional return migration coordinators is proactive communication with potential return migrants. Services and available amenities for families (education, learning assistance, Latvian language course etc.), housing (information on available housing funds within public and private sectors), employment and business start-up in Latvia are among the most relevant topics, that successfully encourage return migration to Latvia. ■



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# Third country nationals' integration in Latvia

Expert article • 2427

In Latvia there are various groups of immigrants defined by their citizenship, legal status, and cultural, linguistic and historical background. The most significant factors in the context of immigration and integration policy are one's citizenship and legal status. Following these factors two main groups of immigrants are Latvian non-citizens (former USSR citizens who did not have Latvian or any other citizenship) and foreigners (people holding temporary or permanent residence permits for different time periods). The group of foreigners, in its turn, is divided into two large subgroups, i.e., citizens of European Union or European Free Trade Association countries and third country nationals (TCNs). Each of those groups has different rights and integration resources depending on their legal status. This review is devoted to TCNs with a temporary or a permanent residence permits living in Latvia based on the comparative research study implemented by *Baltic Institute of Social Sciences* at the end of 2017.

The study of 2017 was the sequential research on studies carried out in 2009 and 2015, which allowed evaluating changes and creating an informational basis for the further implementation of the state immigration and integration policy. As the integration is horizontal policy covering multiple areas of life the aim of the study was to assess the status quo of TCNs in such fields as employment, education, health care, social protection and housing, acquisition of the Latvian language, discrimination, civic participation and interaction with the local society.

According to statistics from the Office of Citizenship and Migration Affairs, the number of TCNs with a temporary residence permit (TRP) and a permanent residence permit (PRP) in Latvia continues to increase (in 2009 - 14 715 with TRP and 34354 with PRP, in 2017 - 26 863 with TRP and 47 977 with PRP which makes in total almost 4% of total population). The most frequent grounds for residence of TCNs with TRP in Latvia are investments in realty (40%), family reunion (19%), work in Latvia (21%) and studies at the Latvian higher educational establishments (11%). The countries of origin of TCNs residing in Latvia are Russia, Ukraine, Belorussia, Uzbekistan, China, India, and Kazakhstan.

The main problematic areas of TCNs integration in Latvian society compared to year 2009 and 2015 still remain the knowledge of the Latvian language, the employment, and the health care. The knowledge of Latvian as the state language is the prerequisite for a successful integration of TCNs into the labor market, education and business development. TCNs have rather high motivation to learn Latvian characterised by the desire to work according to their qualification, intention to obtain a PRP, showing respect for the country of residence and its society, willingness to be part of the local society. Despite the diverse possibilities of acquiring the Latvian language, TCNs still maintain a very high demand for successive and qualitative

Latvian language training at different levels of language proficiency in all regions of Latvia.

Accessibility of health care services essentially differs for TCNs with TRP and PRP. In line with the Latvian legislation, persons with TRP have no right to state-funded health care, including minors. Such right does not apply also to employed TCNs with TRP, irrespective of the effected payments of the social tax, as the national insurance services are attracted not only to effectuation of social contributions (employment) but also to long-lasting stay in Latvia. The problems in the field of employment are mainly caused by the insufficient knowledge of the Latvian language (according to the survey data of 2017 63% of non-working TCNs would like to work in Latvia, 40% are working in the appropriate occupation, 22% of the respondents work in a similar occupation and 16% in another occupation).

Regardless of the fact that compulsory pre-school and primary school education is established by the Latvian law, free general education was not available for a long time to the children of TCNs. Since 2010 the amended Education Law granted TCNs a right to free compulsory education, thus essentially improving the accessibility of education to the immigrant children. There is a systemic support frame developed during the last decade for schools, teachers and parents to facilitate the integration of children with a migration background into school in Latvia. Besides, education in Russian or bilingual is still widely available in Latvia, thus facilitating the integration of those TCNs whose native or intermediate language is Russian.

The core policy recommendations deriving from the study of 2017 are: to extend the support of the state and local governments to the acquisition of the Latvian language; to support declared employment and respect for labor rights at all levels of skills and qualifications of TCNs; to ensure the access to state-guaranteed health services for underage TCNs' children; and to improve access to information about immigrants' rights, duties and opportunities in Latvia. ■

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# The Baltic States: Affluent societies?

Expert article • 2428

In 1958, John Kenneth Galbraith published his famous book *The Affluent Society*, in which he portrayed the United States as being wealthy in the private sector but poor in the public sector, with inadequate social and physical infrastructure, and persistent income disparities, all due to a lack of public investment. Affluence, in Galbraith's perception, concerns private, often luxury, consumption goods, rather than –basic– public services. Public poverty exists amidst private wealth.

In July 2018, as part of the European Semester of economic policy coordination, the European Council issued various economic policy recommendations to Estonia, Latvia and Lithuania. For all three Baltic countries, the European Council pointed at the inadequacy of the social safety net, at the high at-risk-of-poverty rate (especially for people with disabilities and older people), at major deficiencies in public services delivery, and at the relatively huge income inequalities. This assessment largely echoes Galbraith's depiction of affluent societies.

In both academic and political circles, the Baltic States (and especially Estonia) are often seen as exemplary in terms of their earlier transition to open and dynamic market economies. They complied with the EU's accession requirements rapidly, performed very well before the economic crisis, and acceded to the EMU despite of being hit very hard by the crisis. Public debt levels for the three countries are the lowest of all Eurozone members. At the same time, the economic crisis brought out severe weaknesses. The Baltic economies had little to offer in terms of automatic stabilizers, because of ill-developed social security systems. The necessary austerity measures added to income inequalities, made public investment (which was already low) fall, and had a huge impact especially on public sector wages and public services delivery. Obviously, the three Baltic states cannot be expected to rapidly develop a full-fledged Nordic welfare state model, as is found in some other countries in the Baltic Rim, provided that such a model is deemed to be desirable (which as such is questionable and depends on one's political preferences). Still, some sort of welfare state model is needed, even if only as a buffer to lessen the blow of economic crises. What would be the key elements to move towards such a Baltic social model?

First, public investment should be raised. Public investment is understood here broadly, and includes for example investments in physical (transport) infrastructure and investments in human capital. Although some improvement has been made in these areas, the catching-up process here is still very much on its way, with low progress. Moreover, public investment in the three Baltic States depends very heavily on resources made available externally, i.e. from the European Structural and Investment Funds. They are not being derived from the internal economic base, and are the result of opportunities made available by the EU, rather than from own choices concerning the role of government in the economy. In that regard, the three Baltic States also seem to comply unquestioningly with the EMU rules on public deficits and debts, but these rules are detrimental to raising public investment. The OECD has rightfully called their strict application into question, for example in the case of

Estonia. It argues that Estonian fiscal policy has been too tight and that more fiscal space should be used. Fortunately, to some extent the Estonian government has already started to ease the fiscal reigns, by accepting small budget deficits in the years to come, and by spending more on infrastructure, health care, education and family benefits. This approach should be enhanced, also in the other two countries. Contrary to the Brussels paradigm, having fiscal deficits (and creating some public debt) as such is not bad, provided they are linked to investments from which future generations of taxpayers profit.

Secondly, taxation is key to change the balance between private abundance and public poverty. Overall, the three Baltic States have tax burdens which are among the lowest in the EU. Tax levels can be raised significantly to provide more public resources, without jeopardizing the competitiveness of the Baltic States. Taxation is also essential to tackle large income inequalities. Currently, a relatively large role for consumption taxes, in combination with flat indirect tax rates, results in tax systems that are far from progressive, and according to some experts even regressive. Again, some changes have recently been made in all three countries (mainly by increasing the tax-free threshold in the personal income tax), which move tax systems in this direction. However, the steps seem to be relatively small and consequently have low impact.

Finally, the role of subnational authorities should be strengthened. Local governments are essential for public service delivery and have a large role to play in public investment. In all three countries, central government is very strong, and local government is relatively weak. Administrative reform has focused on upscaling local governments by means of (voluntary or forced) mergers. Although such upscaling is important to enhance the administrative capacity of local governments, it does not fundamentally change their role. For that, they should have a bigger stake in the fiscal pie: more financial means through larger intergovernmental grants, and more tax autonomy. ■



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# The Euroscepticism in the Baltic States: Manifested and latent

Expert article • 2429

**T**he objective of this text is dual. On the one hand, we will look for causes and explanations why the level of Euroscepticism in the Baltic states is lower than the European Union average. On the other hand, we will try to identify the fundamental qualities of the “Baltic” Euroscepticism.

To understand and explain why the Euroscepticism of the Baltic states is weak is not that difficult. It is sufficient to take into consideration several important objective factors such as the historical experience, geographic location and the size of the countries.

It is possible to sum up the historic experience by the fact that although in 2018 the Baltic states celebrate their centennial, half of that time they spent under the occupation and differently from Finland could not develop freely and independently.

The geographic location of the Baltic States is also controversial. On the one hand, huge possibilities for prosperity lie in it, but, on the other hand, it hides great dangers. Huge prosperity possibilities are associated with the fact that the Baltic states could be participants-intermediaries of the exchange between Europe and Russia. On the other hand, the collapse of their independence in 1940, when their successful economic, social and cultural development lasting from 1918 was brutally interrupted, just testifies how dangerous and fragile their situation is.

In other words, a lot depends on broader systemic factors. The Baltic states themselves can do little in this situation. The restoration of the Baltic states' independence in 1990 was a real miracle that until then very few expected. However, the restoration simultaneously meant the reemergence of the old worries and problems. Fortunately, the restored second Baltic republics “found” a completely different Europe from the one they “had left”. In 1940, the Baltic states “left” the Europe that had not any powers or institutions that could have helped them to resolve their security problem and stop the raging aggressors. However, in 1990s they “found” a new much more favorable international environment. And the EU is one of the most important building blocks of it.

Therefore, opposing the EU for the Baltic states would equal to losing their sound mind. At present, the existence of such structures as NATO or the EU is an existential interest for the Baltic states. The political elite of all the countries without greater hesitations chose to seek the EU membership and, since they became members of the EU, they have always supported the unification of Europe. Lithuania was the first to ratify the Treaty establishing the Constitution for Europe. Latvia and Estonia did the same notwithstanding that the Treaty had already been doomed. In spite of the fact that the crisis in Greece tarnished the reputation of the common European currency, the Baltic states, as soon as they met the Maastricht criteria, became members of the Eurozone (Estonia in 2011, Latvia in 2014, Lithuania in 2015). Civil societies of the Baltic states have always been and remain pro-European. The referendums on the membership in the

EU won with the great landslide in all the countries, while the public opinion constantly demonstrates a greater trust in the European than in the national institutions.

On the other hand, if everything were so simple, then there would be no explanation why in the Baltic states a certain level of Euroscepticism (although smaller than in other countries) still exists. The answer to this question would be dual distinguishing two main forms of Euroscepticism in the Baltic states – manifested Euroscepticism and the latent Euroscepticism

The *manifested* Euroscepticism in the Baltic states is actually slight due to the afore-mentioned circumstances. In the referendums on the EU membership voted “No” in Lithuania – 8.9 %, in Latvia – 32.5 %, in Estonia – 33.2 %. The greater opposition in Latvia and Estonia is usually explained by resorting to more numerous Russian minorities in these countries. The reasons for this type of Euroscepticism in the Baltic states most probably differ but little from that in other EU member states. Like in other EU member states, the manifested Euroscepticism that reveals itself in the Baltic states can be divided into hard and soft forms.

In case of the Baltic states, hard Euro-sceptics tend to refer primarily not to the most pleasant experience of the Baltic states' existence in the Soviet Union. When the Baltic states prepared to enter the EU, Euro-sceptics invited to drop this ambition putting forward arguments that the European Union is the same “camouflaged” Soviet Union just waiting to transform the republics that have restored independence into its colonies. Still, even now, when the EU membership of the Baltic states has reached the middle of the second decade, this political trend has not completely disappeared. A series of 2010–2015 EU crises itself provide new impulses to the hard Euroscepticism. Hard sceptics have an opportunity to return to their favorable argument of identifying the EU with the USSR again. Yet now they prophesy that, sooner or later, the fate of the USSR is awaiting the EU – the latter will crumble just as the former has done. Brexit has become the most suitable argument for them. The Referendum organized in 2014 on the ban to sell land to foreigners most probably can be regarded, at least in Lithuania, as their greatest achievement. After the voting, the Referendum was declared null and void because of low (14.98%) turnout. However, it was valuable because it demonstrated of approximately what extent the social base of Euroscepticism is.

Soft Euroscepticism, that publicly criticizes not the EU as such but certain aspects of its public policy, in the Baltic states as, most probably, in other EU member states, rests on economic interests rather than beliefs. In case of each of the Baltic State it is possible to find the decisions of the European Union that were not popular with societies of the countries and were met with public debates or even public actions. For example, in Estonia the decision of the European Commission regarding the illegitimacy of state support to the “Estonian Air” was treated very negatively; in Latvia – considerable

attention has attracted the dispute over pay of Latvian construction company “Laval” workers in Sweden; in Lithuania, much controversy was provoked over the EU requirement to close the Ignalina nuclear power station followed by arguments concerning the financing of the dismantling process. Baltic farmers are also dissatisfied though they get the greatest benefit yet think that they are incorrectly wronged as the allowances they receive are much smaller than the European Union average. The list of similar examples could be endless.

Speaking in general, the Baltic states, in terms of Euroscepticism, differ but slightly from other states. However, one difference should be mentioned. Soft Euroscepticism, that in the Baltic states is more expressed not by the official structures but by business or civil society, is rather dampened down because the advantages of the EU membership (security, cohesion policy), notwithstanding all the tensions, in the Baltic States obviously outweigh those costs and inconveniences. Therefore, Baltic societies still put up with EU rules and unfavorable resolutions. For example, contrary to Visegrad countries, the Baltic states agreed with the decision on the refugee acceptance quotas in spite of the reservations expressed by civil society.

Thus, in the Baltic states, both the forms of *manifested* Euroscepticism are rather weak. However, rounding up it is worthwhile mentioning that it would be erroneous to think that the Baltic states are unconditionally Euro-enthusiastic, that their societies, political parties and parliaments are populated by Euro-federalist. It is nothing like that. Just as there is no more influential Eurosceptical movement or a political party, the Euro-federalists of the Baltic states are also equally weak. Those that most experts call Euro-pragmatists obviously dominate in the Baltic states. However, in our opinion the Euro-pragmatists should be called truly genuine Euro-sceptics. Only their Euroscepticism is not *manifested* but *latent*.

We would apply the term *latent* Euroscepticism to such an approach that essentially accepts the present EU but is not actually interested in the continued deepening of the integration. The leaders of the Baltic states have emphasized more than once that they are

rather for the intergovernmental but not supranational Europe. The Baltic states are enthusiasts of the international institutions where they have “a place at the table” but they skeptically assess the granting of new powers to supranational institutions. The Baltic states do not support the sanctions proposed by the European Commission to Poland. The Baltic states are also among those countries that are suspicious towards the reforms proposed by the President of France Emmanuel Macron and did join the rallied by the Netherlands member states’ opposing “club” that the *Financial Times* called the “Hanseatic League 2.0”.

Thus, the choice and position of the Baltic States is quite clear but at the same time problematic. The controversy lies in the fact that they seek to coordinate two things that can hardly be coordinated. On the one hand, the existence of the EU is their existential interest. The Baltic states have always sought not only to become members of the EU but also to participate in all the projects including the Eurozone or PESCO. On the other hand, being latent Euro-sceptics they take the risk of encountering a hard-to-resolve dilemma in case France and Germany, that make the nucleus of the European Union, would agree to move towards a deeper integration or even federation. ■

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# Role of education in regional development: A case of Ventspils

Expert article • 2430

**D**ecrease of inequality between Latvia and EU average based on GDP per capita, competitiveness of labour force, level and development of entrepreneurial activities as well as other indicators is one of the main challenges for Latvia on macroeconomic level. Minimizing the gap of development between the capital city Riga and other regions and territories in Latvia is important task on the country level. One of the solutions is determination of niches for competitiveness in each region which can foster polycentric development of Latvia and restrict growing depopulation within regions of the country.

Attraction of foreign direct investments is an important solution for long-term sustainable regional development in Latvia which is closely linked to creation of business and/or special economic zones. Moreover, each created business zone offers new workplaces, and one workplace in industrial zone creates additional three workplaces linked to education and services. There are a number of successfully developed business and/or industrial zones in Baltic Rim countries including Finland and Estonia. Apart from efficient infrastructure which includes access roads, energy and water supply, high speed internet and other factors, availability of qualitative and well-educated workforce is crucial factor for competitive industrial zone within the region.

Seaport city Ventspils and its special economic zone created by the Ventspils Free port and Ventspils city council is a successful example of regional development in Latvia. During the last decade Ventspils special economic zone has attracted more than twenty foreign companies specialized in information technology, electrical engineering, metal processing and other industries. Ventspils has also designed and implemented development strategy for the city and the region where the main emphasis is placed on the rapid increase of information and communication technology industry. In order to reach the above strategic goal education plays the utmost crucial role.

Ventspils primary and secondary schools, Ventspils Technical College (VTC) and Ventspils University of Applied Sciences (VeUAS) as well as several centers of vocational training form the core of education in the city and the region. It is essential that pupils of the primary and secondary schools from the very beginning of their education has close linkage with the VTC and VeUAS by participating in different interest groups and summer schools related to science, technology, engineering and mathematics (STEM) organized by the above mentioned stakeholders. Furthermore, in order to supply the growing demand for workforce from the companies with foreign investment in Ventspils (i.e. Bucher Municipal, Hansamatrix, Malmar Sheet Metal), VTC implemented new study programmes in metal processing, electrical engineering and information technologies and therefore, increased the number of students in the technical college.

Ventspils University of Applied Sciences will face the most crucial challenges over the next few years because industries within the city and the region urgently need highly qualified workforce with

bachelor and master degrees especially in information technology and electrical engineering. Development of new, multidisciplinary niche study programmes together with leading local and global higher education institutions (HEI) is one of the opportunities to attract motivated students from Latvia and abroad in order to actively react to the demand from the industry. Big data and artificial intelligence, digital business and innovations, team entrepreneurship, efficient use of machine translation are examples of areas the university is working across its faculties of business, translation and information technology. Enriching existing curricula with new study approaches including learning by doing and reverse classroom education as well as more active involvement of local and global practitioners and representatives from the industries is another task for the university. Continuous collaboration with the business incubators, business accelerators, business coaches and trainers will also help to prepare professionally skilled and knowledgeable graduates. Research and development opportunities should be available for the students, and Ventspils International Radioastronomy Center and Smart Technology Research Center along with companies will be the crucial players for development and implementation of new products and solutions. Finally, the Lifelong Learning Centre of the university should act more aggressively towards continuous training and re-training of the workforce because it is important aspect for the companies in the city and the region to remain competitive in the market.

Latvia similarly as other Baltic Rim countries is facing reforms in education system. The number of HEI in Latvia is high comparing with Estonia and Lithuania. Nevertheless, the existing regional universities in Latvia should remain and should be further developed as the strategic goals set for successful growth of a region can be reached only if the regional university is one of the key stakeholders. ■



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# Cross-border vocational education and training

Expert article • 2431

As part of the Copenhagen process, in 2002, European ministers and the European Commission agreed to intensify the cooperation between stakeholders in VET. In particular, the prioritized fields of action include the transparency and recognition of qualifications across national borders. Under the purpose of designing transnational, vocational curricula, questions regarding validation and national recognition are focussed. Using the European instruments EQF and ECVET, the project BBVET - *Boosting Business Integration through joint Vocational Education and Training (VET)*, financed by the *Interreg South Baltic Programme*, attempts to pilot cross-border training for the mechatronics vocation and the educational qualification *Educational Technology*. The premise of understanding the Baltic Sea as a connecting element between the neighbouring regions and to revive historically grown intensive trade relations is the occasion for designing and piloting cross-border vocational training programs.

BBVET is pursuing the EU's goal of increasing VET mobility up to 10 %. Long-term mobility in VET will be used to rebuild or expand economic cooperation in the South Baltic Region. However, BBVET aims not only for a bi-national exchange of future professionals, but also pursues a multinational approach, as the participating students attend classes and training in up to four countries within a one-year-education as part of their cross-border training, which was jointly developed by all project partners. The project started in October 2016, the piloting of the cross-border education in January 2018. The two European curricula are each designed for one whole year, while within this year all four participating countries will be traversed. Each long-term mobility lasts 10 weeks.

The quality-insurance of the cross-border education during each stay is guaranteed by a *Learning Agreement* with the participating learners. The Learning Agreements have been developed by the European Commission and are mainly used for ERASMUS+ mobility. On the basis of *Units of Learning*, the knowledge, skills and competences to be learned for each country are recorded separately and assigned to the respective level of competence in the EQF. Besides the Hard Skills that are covered by the vocational curricula, the educations were also enriched by "soft skill"-workshops due to the intercultural and linguistic aspects. After successful completion of the long-term mobility, the validation takes place in the respective (home) countries. At the end of each country period, learners receive a *Transcript of Records*.

Currently, the project faces many challenges. In the framework of cross-border training, it is imperative to analyse the respective education systems and to understand their genesis and particularities. The development of a European curriculum presented areas of discussion regarding the chronological sequence of subject-related content as well as learning levels. Furthermore, securing the respective recognition is a question that the project consortium is currently addressing. The aim is that the two vocational curricula will be recognized nationally in each project country while using ECVET.

More lobby work still needs to be done in this area.

Partly, the training companies in Germany in particular, announced the fear of a loss of quality in the education itself within long-term mobility. This could be countered with the help of the *Learning Agreements*. The project also tries to remedy the question of "knowledge and competence growth" within long-term mobility by carrying out soft skills measurements, which are anchored in the curricula in addition to the hard skills. Another goal in the project is the establishment of so-called mobility agencies in order to consolidate the already developed know-how regarding long-term mobility and to have front runners that can show success stories, so that more VET educations dare to invest time in working internationally with long term mobility.

Even though, the project just passed the mid-term of piloting of the cross-border educations, there are already a lot of achievements that can be stated. Having the focus on smaller regions, through the cross-border cooperation there is a chance to highlight their attractiveness and draw new talents that are coming to the region. The project has proven to be very successful, following the example of the German education system, to combine theoretical subjects in schools with company internships during transnational education. This also increases stakeholder cooperation in the regions itself. Additionally, reactive, it strengthens markets and increases competitiveness. For the students, it is a great learning process to start very early in their education to work in an international team, learning about the market in each country. The participants are ambassadors for their countries and stimulate European exchange, both at an intercultural and vocational level.

By opening up the educational systems, the posted students can network within the international labour markets more intensively. This ensures that the countries of the Baltic Sea region merges together more and more. The demand for vocational mobility seems to be very high and is increasing due to the activities in the project. The work in the project has shown that it is possible to innovate national VET systems through European cooperation. ■



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# Digital industrial platforms as enablers of a closer Nordic integration

Expert article • 2432

**N**ordic countries are world leaders in innovative solutions and direct applications in different sectors including industries. According to the Global Innovation Index 2018, Sweden, Finland and Denmark rank among the top 10 countries since last five years and are among the key players energizing the world with innovations. Innovation investments transformation into results is a key factor for a sustainable success where information technologies are an imminent part of innovations.

Nordic region is world known with its state-of-the-art industry, pioneering technologies, innovation and research, world famous companies. Industrial internet and Industry 4.0 concepts emerge. Expanded forms of effective cooperation are required between suppliers, manufacturers and buyers. In order to remain competitive, industries constantly demand reliable partners with competence, skilled personnel and industrial knowledge, sustainable business strategies, international business development and networking.

To facilitate this movement, a number of digital industrial platforms have been developed and are driven by Nordic business. They have sectoral approach as packaging, engineering related and act as enablers and springboard for further development and growth by matching manufacturers, equipment and stock item suppliers, buyers.

Despite a wide and even global on-line application of inventions, a geographic proximity can play an important role to test, get critical mass of users, apply and make these solutions functioning on business mode. Neighbouring Baltic region countries are suitable partners being on this overall innovation ranking in the third-fourth ten (Estonia, Latvia, Poland, Lithuania). Regional cooperation is an ideal bridge to link innovations and application. Mutual benefit, fully fledged complementarity to invent and apply, right integration in value chain, focus on results, minor impact of cultural differences, these are important factors where the region can combine and use modern solutions, synergy and implementation of win-win strategy.

Facilitation is not a new business idea. There is a variety of enablers as trade fairs, matchmaking session, public institutions, private consultants with strong footprint in the Nordic region for industrial sectors. However, all business models have to be reviewed and adjusted continuously as new business tools and applications emerge, next gadget oriented generation joins business, time is precious, resources limited, competition fierce.

Usage of digital platforms needs to be promoted as well. Some companies owning such platforms leave their marketing just purely for on-line way including direct where some of them use in-house support or agent network by applying human factor to promote and explain the essence of benefits to use one or another platform. Naturally, such human intervention is more likely on geographic proximity where customers understand offered service easier and quicker.

European Union companies including Baltic region benefit from EU structural support to promote and attend trade fairs. This can be a suitable way, but it can be costly too, in particular for start-ups and small companies. In addition, trade fairs adjust their business by launching new tools which have been used at smaller degree earlier: parallel matching sessions, enhanced on-line entries, new products buyers guide and distribution to potential visitors to promote attending companies.

Some of such world digital platforms possess a global approach with tens of thousands members (suppliers, traders, manufacturers dealing with subcontracting, equipment or stock goods) world-wide. How to be specific and advanced in a such large number of members where any competitive and specific advantage can disappear or melt or many other factors can play more important role of partner selection as its size, supply speed, transportation costs, communication language, cultural awareness? It is rather challenging to build Baltic company profile in another corner of the world even using on-line channels. As alternative and start can be considered Nordic companies interested for partnership where business facilitation is supported by these digital industrial platforms. Baltic benefits can be as just one hour flight, high quality offered, education and engineering potential are existing at appropriate level, goods can be shipped overnight, rework and maintenance can be done quickly and under minimal costs. Hence, Nordic business partnership can be a suitable mutual cooperation facilitated by digital industrial platforms.

Regional cooperation can be a right model to start and grow by using traditional and emerging and growing business solutions as digitalization: innovations are created, offered and applied on mutual approach by making the region can be stronger together. ■

**SIGITAS BRAZINSKAS**

Expert, projects funded by the  
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ALEKSANDR IZGORODIN

# Lithuanian manufacturing: Rapid growth accompanied by challenges

Expert article • 2433

There is no better word than “critical” that would describe the importance of manufacturing to Lithuanian economy. Manufacturing is the biggest sector of Lithuanian economy, generating slightly more than 20% of Lithuanian GDP and almost 80% of exports. Eurostat data shows that in 2017, export of goods accounted to 62% of Lithuanian GDP, which is almost two times higher than the EU average (33%).

Currently, Lithuanian manufacturing is enjoying a “golden” period, which can be illustrated by such aspects as fast growth in output and record capacity utilization level. For example, over the last 5 years, production output in Lithuanian manufacturing rose by 33% and is more than 50% above the pre-global financial crisis level. Currently almost 80% of total manufacturing capacity is fully used, and this number stands at historically highest level ever. The secret behind this numbers is simple: 80% of export of Lithuanian goods goes to the EU region, which is enjoying a period of sustainable growth. In addition to this, Lithuanian manufacturing businesses are becoming more integrated into the European manufacturing value chains and receive contract manufacturing deals from EU businesses.

However, there also several challenges that lie ahead, and the future of Lithuanian manufacturing will depend on abilities of businesses to withstand these challenges.

**1. Lack of workforce and rapid wage growth.** Chronic lack of workforce has affected Lithuanian manufacturing mostly through the labor cost side, as in the last 5 years salaries in manufacturing rose by almost 40% (increase in minimal wage also had an impact). However, it seems that currently Lithuanian manufacturing sector is able to withstand this challenge rather well. Companies are increasingly focusing on processes that would help increase the efficiency – and it worked: Lithuanian manufacturing is producing 43% more goods than before the financial crisis but will 14% smaller number of employees. In addition to this, although a 40% increase in labor costs sounds risky, in fact if the growth in wage is displayed in EUR/hour, Lithuania occupies only 11<sup>th</sup> place in the EU in terms of wage growth. Salaries in Germany and Denmark over the last 5 years increased twice as much as in Lithuania (3,6 and 3,3 EUR/hour in Germany and Denmark respectively vs 1,7 EUR/h in Lithuania).

**2. Lack of innovations in manufacturing.** One of the major challenges to Lithuanian manufacturing sector comes from the structure of Lithuanian manufacturing itself. 75% of added value, sales and production output of Lithuanian manufacturing is generated by low and medium-low technology sectors – which employ 85% of all employees that are occupied in Lithuanian industry. While Lithuanian manufacturing is registering a blistering pace of growth, this growth comes from low-tech sectors. Data from the Eurostat shows that one employee in Lithuanian manufacturing currently generates 19 ths

EUR of added value per year, while the EU average figure stands at 62 ths EUR. Increasing these numbers will require an effort from both the business sector and authorities.

**3. Automatization and digitalization of industry in Europe (Industry 4.0).** Up until recently, the “industry 4.0” term was not a well-known term and was not used too often in the business vocabulary. Things have changed, however and a few simple examples clearly show that the fourth industrial revolution in Europe has already begun. In Denmark, production in manufacturing rose by 23% after the global financial crisis, while the number of employees in manufacturing dropped by 5,5%; In Belgium, production in manufacturing rose by 15,4% after the crisis, while the number of employees in manufacturing dropped by 12,3%. The share of manufacturing sector in total employment in Belgium declined from 16% in 2008 to 12% in 2017; Germany registered a decline from 21% in 2008 to 19% in 2017. In Finland and Sweden the declines are even more rapid: in Finland the figure dropped from 16% in 2008 to 13% in 2017, while in Sweden the share of manufacturing sector in total employment decreased from 14% in 2008 to only 10% in 2017. These are only several examples that demonstrate the fact that European manufacturing sector has begun its transformation towards higher levels of automatization. Automatization will clearly have an impact on business relations between Lithuanian and bigger EU manufacturing businesses – therefore, Lithuanian companies must quickly react to the structural changes in the EU and start putting more effort towards investments into smart equipment and smart manufacturing processes. On a positive note, the level of capacity utilization in Lithuanian industry (78%) currently is at historically highest level ever, and businesses are planning new investments into equipment as well. Therefore, now is the right time to invest not only into increase of manufacturing capacity, but also into ultra-modern equipment and processes. ■



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ALEXANDRA MIDDLETON &amp; ANDREY MINEEV

# What are the business opportunities and development challenges in the Arctic?

Expert article • 2434

**T**he Arctic is attracting attention from the business community. The opening of the sea ice creates a business case offering improved accessibility of Arctic natural resources. The Arctic needs sustainable business solutions that are respectful of the environment and ecosystems in the Arctic. Natural and environmental sciences currently dominate discourse on the Arctic. Decision-makers lack systemized and reliable business-related information that covers the Arctic countries.

The Business Index North (BIN) project financed by the Norwegian Ministry of Foreign Affairs, Norland County Council and implementing partners fills this business information vacuum. The BIN report is a knowledge-based, systematic information tool for stakeholders such as businesses, academics, governments and regional authorities, as well as media in the Arctic states. The partners contributing to the project are familiar with local conditions at first hand. The report covers eight northern regions of Norway (Finnmark, Troms, Nordland), Sweden (Norrbotten and Västerbotten), Finland (Lapland, Northern Ostrobothnia and Kainuu) and two Russian regions (Murmansk and Arkhangelsk regions).

To understand preconditions for business development in the Arctic, investors and business need to have a clear picture of socio-economic trends the region. BIN provides a set of indicators and indices that measure socio-economic development in the Arctic. These indicators reflect demographic and human capital trends, employment, business, innovation potential, maritime transportation and connectivity in the North.

The population in the north of Norway, Sweden and Finland has experienced disproportionately slow growth the last ten years, being 2.7 times slower than in the respective countries overall. Cohorts of youth (0-19 years) and working age population (20-64 years) have declined in the North, while the elderly population aged 65+ is on the increase. This reflects the growing share of baby-boomers in the population and inability to increase population through domestic and international migration mechanisms. The Russian regions of Murmansk and Arkhangelsk are experiencing shrinking population as a consequence of post-1990s socio-economic transformations. Who will be living and working in the North in the next decade if the same trend continues?

Human capital measured in terms of tertiary education attainment predicts future earnings and the health of individuals. In the north of Norway, Sweden, Finland, male population with tertiary education lags by 6 and female by 3 percentage points behind the respective national averages. Murmansk and Arkhangelsk regions are experiencing the same trends. Is this a problem? In future automation will require more high-skilled workers, so the discrepancy in tertiary education attainment may lead to an insufficient pool of job seekers in the north. This constitutes a risk for business activity in the Arctic. It is policy-makers' role to address this issue by providing competitive and diversified education in the Arctic.

Employment in the north of Norway, Sweden, Finland has shifted

from traditional sectors of mining, quarrying and manufacturing, agriculture, forestry and fishing to a service economy dominated by human health and social work activities that accounts for 22.1% of all employment. In the Russian regions of Murmansk and Arkhangelsk the mining, quarrying and manufacturing industries served as the second biggest employment provider, but experienced job losses during the period 2012-2014. The Norwegian, Swedish and Finnish North experienced a loss of nearly 5,000 jobs in mining, quarrying and manufacturing during the period 2012-2016.

The report demonstrates that innovative businesses build upon the Northern identity and values often associated with fresh and clean water, air and food, majestic nature, outdoor activities and active lifestyle. Examples of innovative clusters include aquaculture in the north of Norway, data centres in Kajaani and Luleå, health technology in Oulu and a growing sector of Arctic tourism in Northern Russia. The BIN report analyses the development of maritime transportation via the Northern Sea Route (NSR). The total volume of cargo transported along the NSR grew by 42% from 2016 to 2017, dominated by Russian internal traffic. Transport of natural resources out of the Arctic is expected to be the main driver for NSR development.

Reliable and fast internet connections are vital for businesses. The North of Norway, Sweden, Finland and Russia is performing well in terms of basic broadband availability, while lagging behind in high-speed broadband. Mobile broadband coverage is insufficient in the unpopulated areas in the Arctic. The European and Russian Arctic lacks direct subsea data cable connections with the rest of the world.

The Finnish Chairmanship in the Arctic Council 2017-2019 sets the following priorities: environmental protection, connectivity, meteorological co-operation and education. All equally important, we shall remember people and concrete sustainable business opportunities when addressing development in the Arctic. ■

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AKI PULLI

# Ukraine's increasing presence in Baltic region

Expert article • 2435

**T**he events in Ukraine in 2013 – 2014 had a major effect to the orientation of the country and following both the Revolution of Dignity and the Russian aggression in Crimea and Donbas, including the ongoing warfare, have changed Ukraine's political and economic orientation drastically. That is also felt in the Baltic Rim.

The Baltic Rim country traditionally closest to Ukraine, Poland, is having currently some 800 000 Ukrainian legal residents, while unofficial figures are higher. On the Polish Baltic Sea shores, in the Pomeranian Voivodeship alone, in 2017 all in all 216 000 work permits were issued to Ukrainian citizens. That is equivalent of all Lithuanian population living near the Baltic shores. Same effect, in lesser extent, has been taking place in all Baltic Rim countries, even Russia. The number of Ukrainians in all countries has grown, thus increasing grassroot level connection between Ukraine and countries in question. From the Soviet times, Ukrainians have been a small, but considerable minority in the Baltic States, but now there is new migration. In Estonia, Ukraine has surpassed Russia as the prime country of origin for new residence permit holders, and similar trend is being seen also in southern neighbours Latvia and Lithuania. Whereas the migrant workers from Ukraine to wealthy Scandinavian countries used to be predominantly highly-educated people, the situation in last years has changed drastically. Low-qualification, rather physical jobs not popular among the locals, often in the agriculture, is the main attraction for Ukrainians now arriving to Denmark, Norway, Sweden and Finland.

The key elements in increasing the trade between Baltic Rim countries of the EU have been the change of political course in Ukraine as well as some economic reforms that have been implemented since 2014. Most drastic game changer in trade has been the Association Agreement between Ukraine and the EU, which has made trade easier and lowered the existing barriers. The Deep and Comprehensive Free Trade Agreement (DCFTA) that has been in provisional use since beginning of 2016 and officially implemented since 1<sup>st</sup> of January 2017 has led to some increase of Ukrainian exports to Baltic Rim countries. Alone in the first quarter of 2016, Sweden's export to Ukraine increased by 41% compared to year before. Similar development has been seen in all northern and many other EU countries. Together with increasing flow of people, also goods are moving more and more.

Growing economic and human contacts between Ukraine and Baltic Rim countries has led to growth of transport connections. Flights are regular now from all Baltic Rim capitals to Kyiv. There are several companies operating from Ukraine to transport people and small amounts of goods in minibuses through Poland and Baltic States to Finland. Currently Ukraine is improving its desolate road network in increasing speed and results partly already seen. Belarus is logistically in a pivotal position, as the shortest land route from Kyiv to Vilnius, Riga, Tallinn and Helsinki goes through Belarusian territory

and its capital Minsk. There is already a train connection that has been opened in late September 2018, connecting Kyiv, Vilnius, Riga and possibly later Tallinn, too. Except for the gauge width advantage, the problems with Belarus are multiple. All EU citizens overland need a visa while Ukrainian don't. Border controls take a long time, so while through Poland there is only one slow border to cross, via Belarus there are two slow borders. For road vehicles the strangest road toll system in the world, BelToll, is a hazard. Future political orientation of Belarus remains a major question, too.

Since Ukraine has been victim of the Russian aggression from early 2014, the support from the EU and Baltic Rim countries has been at best lukewarm, except for Baltic States and Poland. Lithuania was the first and so far, the only western country to donate lethal weaponry to Ukraine since the conflict emerged. Other countries, since the initial outbreak of warfare, have slowly changed their course and agreed to sell lethal weaponry, but aid has been limited to non-lethal equipment only. Facing a common threat, also NATO countries in the Baltic Rim that border to Russia have increased their military and security cooperation with Ukraine. Most notably Poland, Lithuania, Latvia and Estonia, but Norway, Denmark and even non-NATO Sweden and Finland. Partly due to growing concern about US and Western Europe's commitment to defend Baltic Rim within NATO framework there have been speculations about reviving the inter-war idea of Intermarium to have better security and defence coordination in the region and as a backup plan if NATO would become dysfunctional. A comparison to early Baltic Intermarium is particularly fitting, as independent Ukraine had its representatives present in the first diplomatic consultations, for instance in Latvian Bulduri in August-September 1920.

There are impediments slowing down the development, primary the corruption inside Ukraine and Russian interference both in Ukraine and Europe, but the direction is clear: Ukraine is already deep involved in the Baltic Rim region and it is not intending to disappear. ■



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TIINA RITVALA

# Grand challenges and the small wins strategy

Expert article • 2436

**T**he world's oceans and seas are essential for us - without them, there is no life on our planet. Despite this fact, the humankind has mistreated the water ecosystem for centuries. The resulting burden is very concrete in our home sea, the Baltic Sea. This summer, the Baltic suffered from the worst algae summer since 2005. Another more global threat is ocean plastic pollution - by the year 2050, the amount of plastic in oceans is estimated to exceed the amount of fish by weight. These collective problems represent grand challenges, societal problems that can be robustly addressed only through coordinated and collaborative effort. But how can we address such complex problems that might seem too daunting for any individual, organization or nation to tackle?

Organization theorist and psychologist Karl E. Weick has reasoned that complex social and environmental problems feel so overwhelming and depersonalized that people feel powerless, which lowers their activity and innovative action. As a result, Weick suggests that organizations and their leaders can adopt a small wins strategy. A small win is a concrete, implemented outcome of only moderate importance that produces visible results. By itself, one small win may seem unimportant, but they have a tendency of deterring opponents, attracting new allies and resources and, thus, increasing the possibility of larger future wins. While Weick admits that small wins may sound hopelessly naïve, they are sensitive to the pragmatics of policymaking as they supplement rather than dominate policy, making them to be more likely to be incorporated in rules, norms and policies. Research has indeed, proven and shown how small wins enable shift in attention and build confidence for new ways of acting, thus energizing necessary change efforts and future action.

An example of a small win is a floating litterbin installed in the water in ports and marinas to collect plastic and other rubbish. The first prototypes of this 'Seabin' were handcrafted by two Australian surfers of plastic rubbish bins, glue and duct tape. The crowdfunding video of this tiny social enterprise attracted quickly over 85 million views raising the interest of global corporations, impact investors and cities around the world. Over 50 marinas and ports in almost 20 countries have installed Seabins, which together are collecting some 100,000 kilograms of rubbish per year. While their environmental impact is arguably minor with respect to the megalomaniacal ocean plastic problem, the awareness raised of the plastic issue is significant. Rather than offering a mere product, the Seabin Project offers a whole solution, including also science, research and education programs. This whole solution has been harnessed in lobbying legislators, as well as, ensuring community and industry participation. A large win will of course, require more resources and the involvement of all parts of the chain from packaging producers to governments, industry and consumers who use and regulate plastic to work towards the common goal.

Similar to the ocean plastic problem, the most severe symptom of the sick Baltic Sea, eutrophication, requires numerous small wins from some 1.5 million farmers of the catchment area of the Baltic Sea. Such tremendous scale requires innovative cross-sector partnerships between farmers, industry, governments, non-profits, research institutes and environmental agencies to mobilize action. In Finland, recent promising collaborative projects include, for instance, gypsum treatment of agricultural fields to reduce the phosphorous load from the fields into the Baltic Sea. At the heart of this project is multi-stakeholder cooperation between private foundations, research organizations, farmers and related associations. In another project, similar form of boundary-crossing networks, including some leading Finnish food and drinks companies are being built to influence individual farmers' behavior by sharing knowledge on sustainable farming practices.

Through their teaching, research, innovation and outreach activities universities are at the forefront of solving sustainability problems of our planet. For instance, students are increasingly educated on how global sustainability goals and principles (e.g. the UN Sustainable Development Goals) may be embedded in business strategies and research programs are designed to resolve ecological and social tragedies.

Since solving environmental issues involve institutional complexities and necessary changes do not take place at a fast pace, small wins strategies are needed—as the popular saying goes: "How do you eat an elephant? One piece at a time". Research has shown that such positive accomplishments associated with small wins strategies may not only form a workable tool to tackle wicked policy problems, but can also function as an important motivational driver for employees. Can you identify and accomplish a small win? ■

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ALEKSANDRA WĄSOWSKA

# Political and social strategies of multinationals in Sub-Saharan Africa: A focus on Polish firms

Expert article • 2437

**M**ultinational enterprises (MNEs), the key actors of globalization, play an important role in the development of both home and host economies. They also often become agents of positive changes in the institutional environment of the countries they operate in. However, they may also behave in a 'socially irresponsible' way, supporting corrupt regimes, and bringing about pollution and human rights violation. Powerful as they are, MNEs are subject to pressures from numerous and geographically dispersed stakeholders (e.g. shareholders, governments, politicians, NGOs, civil society), whose interests are often divergent. Moreover, these interests and the corresponding pressures change in time, as evidenced by the recent rise of economic nationalism and protectionism. Therefore political and social strategies have become critical to MNEs' performance. In essence, the survival and success of MNEs depend more and more on the extent to which governments and other stakeholders perceive them and their actions as legitimate.

Two recent phenomena have become particularly relevant for the analysis of MNEs' political and social strategies. First, with the rise of outward foreign direct investment from China, India, Brazil, and other developing countries, a 'new breed' of emerging market multinationals (EMNEs), have populated the world economy. Among them, there are firms from post-transitional economies of Central and Eastern Europe, searching for their place in the global markets. MNEs from emerging markets are typically smaller and less endowed in traditional ownership advantages, such as brands and technologies. However, they do possess some assets and capabilities that benefit their internationalization. For example, EMNEs are able to develop 'good enough' products, offering reasonable quality at affordable cost. Moreover, they know how to operate in difficult institutional environment at home, and they may transfer this experience abroad. Many of them are state-owned and enjoy a privileged position in their home countries, receiving a considerable governmental support for their foreign expansion. In sum, EMNEs build their competitive advantage based on a different set of capabilities than developed country MNEs, often recurring to political strategies and resources.

Second, some of the least developed regions, such as Sub-Saharan Africa (SSA), have increasingly attracted FDI, thus becoming an economic battlefield for developed and emerging market multinationals. Both these groups experience, however, serious legitimacy threats in SSA, facing accusations of neo-colonialism, human right infringements, and degradation of environment. Some examples of political and social tensions provoked by MNEs' operations in SSA include controversies around Brazilian investments in Angola, Mozambique and Guinea-Bissau, anti-Chinese sentiments in Zambia, as well as widely discussed cases of corporate

irresponsibility of Western MNEs, including the activity of De Beers in Botswana and Royal Dutch Shell in Nigeria.

MNEs from CEE have typically entered markets which were geographically, culturally, and institutionally close to their home countries. Recently however, an increasing number of firms from CEE have ventured globally, particularly to SSA. Among them, there are several Polish firms, including Asseco (IT services sector), Kopex (mining machinery), Kulczyk Investments (diversified group, involved in extractive operations in SSA), Lubawa (woven and knitted fabrics), Navimor International (projects for the maritime sector), Pietrucha (geosynthetic products used in civil engineering), Ursus (agricultural machinery), Wielton (semi-trailers). This is due to many factors, including shrinking margins, rising consumer expectations and more and more demanding environmental norms in developed markets, as well as the emergence of a new generation of entrepreneurs and managers, who are adventurous enough to go truly global. Expansion of CEE firms to Africa has attracted attention of the media and think-tanks, who suggest that these companies seek to renew historical ties between CEE and SSA, and that the transformation of CEE towards market economy may serve as a role model for SSA countries. The expansion of CEE firms to SSA has also been supported by the government-sponsored initiatives (e.g., 'Go Africa' launched by the Polish Ministry of Economy). Overall, the dominant narratives about the potential of SSA for CEE companies have been optimistic, despite some examples of failed investments from CEE (e.g., the Polish copper and silver conglomerate KGHM in Congo). However, despite a great market potential of the region, poor infrastructure and institutional challenges may pose severe constraints for the economic cooperation between CEE and the SSA countries. Even if, as latecomers, CEE firms can learn from the pitfalls of other MNEs operating in SSA, they will probably make their own mistakes. In any case, they will need to seriously think about their political and social strategies to establish legitimacy in SSA. ■



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# Cuba attracts more than ever – Bokira's view

Expert article • 2438

**E**merging market of the globe keeps on attracting interest not only from the business point of view but also from the social impact and sustainability point of view. Capital intensive projects like infrastructural or energy generation are linked with a certain degree of risk. However, one common denominator is present: there is a need for funding instruments through joint ventures where risks, responsibilities and rewards are being shared. In addition to the right contacts also long term commitment, building trust and being present are basic foundations for success in emerging market.

In Cuba the situation is not much different from the rest of the developing markets. The presence of state monopoly together with opening of the Cuban market for foreign industrialists and investors deliver huge business opportunities: for those who can afford the risk, allow time consuming procedures, do not expect quick rewards and above all, manage to build trust all the time. Payment times like 360 and 720 days are reality in Cuba which has an impact on revenue, loss and profit. To succeed it is essential to create solid contacts with the decision makers of the Cuban authorities and the Cuban government owned companies from the very beginning in order to create an open and prompt flow of communication.

Cuba is still a closed economy where the deficit in trade is significant. In the year 2016 the deficit was some 6 billion €: export around 1 billion € and import some 7 billion €. Unfortunately this deficit trend has been increasing. Cuba is in a serious need of foreign currency that would support local investments for local demand and export. Currently import activities are not supported by the Cuban government, resulting in high import duties. This is a fact in all emerging markets where only local manufacturing and job creation is rewarded by the local governments.

In Cuba a promising and increasing business sector is tourism. Cuba is the third-most-visited destination in the Caribbean after Dominican Republic and Puerto Rico. This pushes for investments in real estate, food security, renewable energy, drinking water generation and waste management. For example, 80 % of the food consumed in Cuba is being imported. This opens business opportunities in the food processing value chain and supporting functions like packaging. Needless to say, roads, cruise ship terminals and airports offer all plenty of opportunities too. Companies like Meliá and Kempinski hotel chains, Canadian mining and energy company Sherritt and the French construction company Bouygues have already a strong positioning in Cuba.

Cuban government tries annually to allocate about 2,2 billion € for foreign investments. The free trade zone Mariel outside Havana is offering foreign companies attractive and even tax free conditions

if they start to operate in the zone. Cuban government pushes a lot of joint venture set-ups where the foreign part can even get a major share of the company.

Bokira Group has been operating in Cuba since 2016. Bokira Group is a Helsinki based investment facilitator with a Havana based country representative. The vision is to open new business opportunities for investors, develop Cuba towards clean technology and bring prosperity to Cubans. The business model is based on executive contacts and trust with Cuban authorities and governmental companies, selected investors and companies. The business model is based on setting up a joint venture with the Cuban part where Bokira Group remains as a one shareholder of the foreign part. Until now there are several interesting projects in the pipeline, for example one in packaging sector. In this project the Cuban and Finnish partners have visited each other and negotiations are ongoing in a very detailed level. The Cuban partner is currently working on a feasibility study that will support the investment decision. Bokira Group is being given opportunities for example in hotel business, shipyards and marinas, sustainable transport and mobility, packaging and glass production. In general, Bokira Group is constantly working on projects that are in size above and below 100 million €.

EU has been active in Cuba since 2008 and since 2016 EU has had an active political and economic initiative towards Cuba. Also the future presence of European Investment Bank will further strengthen the ties between Cuba and the EU member states. Currently Bokira Group is contacting dedicated companies in Finland, around the Baltic Sea Region and in EU in order to attract them to Cuba to settle down and grow together with Bokira Group and the Cuban counterpart.

Next year Havana, the capital of Cuba will celebrate its 500 years anniversary. Cuba has its momentum now. This momentum offers pioneering foreign investors a unique opportunity to build a sustainable future together with Cuba. ■

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KARI LIUHTO

# The future of Cuba: Reform or revolution

Expert article • 2439

**T**he Pan-European Institute (PEI) has been studying the transition from centrally planned economy to market economy for more than three decades. With the help of a grant from the Foundation for Economic Education (Liikesivistysrahasto), the PEI began to investigate this transition in Cuba a few years ago.

In late June, I attended an industrial trade event held in Havana. The event opened with a panel discussion that was chaired by a man wearing a Fidel Castro-style military uniform. The two key speakers of the panel were from China and Russia. No representatives from the European Union were present at this opening session, even though there were numerous exhibitors from the EU at the fair. I also met a handful of Finnish businessmen at the fair. The absence of **Donald Trump's America** was not exactly surprising.

Prioritising cooperation with China and Russia makes sense from a historical-ideological perspective, but it has no economic foundation, considering the fact that China and Russia put together account for a smaller portion of the global economy than the EU or the USA alone. Another fact worth keeping in mind is that the EU is currently Cuba's largest trading partner, accounting for a third of its foreign trade. Meanwhile, China and Russia together account for only a quarter. But these numbers can change radically, considering Cuba's nearly non-existent foreign trade. Last year, foreign trade was worth less than three billion euros. In comparison, the value of foreign trade in Finland, with a population half the size of Cuba's, was more than 40 times that.

If **Miguel Díaz-Canel**, Cuba's new President just elected in April, will attempt to follow in the footsteps of **Mikhail Gorbachev** and rescue the socialist system instead of seeking comprehensive economic reform, the country will need a generous external funding provider. Cuba will soon run out of financial resources to uphold the socialist system, which came to its end three decades ago. Evidence of the system's failure includes decaying infrastructure, distorted price and salary structure, prices increasing faster than salaries, small product selection and empty shelves in stores, and the large number of inactive people. This, combined with the country's young demographic structure, is a recipe for social upheaval. Unrest is kept at bay by the elite's resistance to change, the opposition's weakness, and the general *mañana* attitude amongst the population.

If Cuba's current leadership strives to build the future of the country on cooperation with China and Russia, the response of Trump's America to Cuba cosying up to the East may be at least as determined as **John F. Kennedy's** was half a century earlier.

But regardless of Cuba's crumbling infrastructure and economy, the country is a unique travel destination. It is a fascinating mixture of colonial buildings, socialist decay, old American cars, and a laid-back Caribbean lifestyle. The dual currency system, which makes prices surprisingly high for tourists, may discourage foreign travellers. For instance, a bottle of the local beer may cost more in a street bar than it does in Estonia. Yet the friendly and hospitable locals with their *joie de vivre*, and street safety, make Cuba an attractive place to visit despite the artificially high prices. If you plan to visit, do it soon, because Cuba is likely to lose its unique charm gradually as globalisation progresses.

Witnessing the country's change first hand was **Ernest Hemingway**, who formed an American counter-intelligence unit in Cuba after the attack on Pearl Harbor. The unit was soon shut down, but Hemingway continued his sociable life and open-sea fishing in Cuba until the accession of **Fidel Castro** in the late 1950s. His years in Cuba are also reflected in his novel *The Old Man and the Sea*, which was published in 1952. A few years later, Hemingway won the Nobel prize in literature. Today, Hemingway's villa outside Havana is a tourist attraction. Its condition is a silent testimony of the achievements of socialism in Cuba. ■

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# BALTIC RIM ECONOMIES

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