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**Research Report**

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## “Friendship” Blockaded

The Russia/Belarus Conflict Is a Post-Soviet Turning Point

Rainer Lindner

By raising the gas price for Belarus, buying a major stake in the Belarussian gas pipeline network, imposing export duty on Russian oil deliveries to Belarus, and restricting duty-free import of Belarussian goods to Russia, the Russians have ended an era in relations between the two states. The heart of the “United State of Russia and Belarus”—the customs union—has been made obsolete at a stroke. Russia’s economic policy toward its western neighbor is part and parcel of a new foreign policy that—as the Putin era comes to a close—is focusing increasingly on the national interest. The Lukashenko system, whose economic and political stability were based on the cheap oil supplies from Russia, has been plunged into a serious existential crisis. For the EU and Germany this renewed disruption to energy relations reveals the fragility of the “strategic partnership” with Russia and the lack of an effective energy dialogue with the transit state of Belarus.

The conflict over Russian gas supplies to Belarus was resolved provisionally on December 31, 2006. This time, unlike in January 2004 when supplies were interrupted, the Kremlin avoided provoking a full-scale gas crisis. Although the agreed compromise price of \$100 per thousand cubic meters is still the lowest in the post-Soviet region, in the long run it is unlikely to be sustainable for Belarus’s state-run economy. According to Belarussian Prime Minister Sergei Sidorsky, the gas price hike will mean closure for about a quarter of the country’s businesses. The central motivation for Russia’s Gazprom is control of the transit pipelines. Gazprom was willing to pay \$2,500 million for half the shares in the

Belarussian state-owned Beltransgas, whose total worth had been estimated a year ago at about \$800 million.

### Russian Interests

Russia’s new energy foreign policy is driven by both economic and political interests: price increases for gas within Russia, Gazprom’s difficulties in meeting its huge supply contracts as gas reserves gradually dwindle, the beginning of campaigning for the 2007/8 parliamentary and presidential elections, and not least the criteria for admission to the World Trade Organization in 2007 (which excludes a policy of favoring neighbors).

On December 8, 2006, the Russian government had already decided to introduce a duty of \$180 per tonne on crude oil exports to Belarus, and the Russian oil corporations passed the increase on directly to their Belarussian customers. Late in the evening on January 7, 2007, the Russian state-owned Transneft stopped oil transport through the "Druzhba" ("Friendship") pipeline to Belarus and the states of the EU on the grounds that Belarus had been illegally taking oil to the value of the transit duty that Minsk had imposed (backdated to January 1, 2007). This charge for allowing passage of crude oil to western Europe—\$45 per tonne and 100 kilometers—was intended to fill the looming hole in the Belarussian budget. On the very same day Minsk offered as a compromise to drop the transit levy if Russia withdrew its export duties on oil. The offer reveals the weakness of the Belarussian side, which had greater economic harm to fear than Russia. On January 10 Belarus withdrew its demand for transit duty.

At home above all, Vladimir Putin himself is seeking to make an impression in the phase leading up to the 2007/8 parliamentary and presidential elections. In the cabinet meeting on January 9, 2007, the President had the responsible ministers enumerate how the oil export duties would reap additional revenues of \$3,500 million for the state budget. Putin's message was: no more gifts of friendship to neighboring states, especially not where the recipients refuse to follow a course of integration on Russian terms. The decisive argument for the Russian electorate is the consolidation of Russia's own budget. In the Ukraine crisis of 2005 Putin was even willing to risk further damaging Russia's reputation in the West as a reliable energy supplier.

### **The End of the "United State of Russia and Belarus"?**

The economic foundations of the "Treaty on the Formation of a Union State" that Russia and Belarus signed on December 8, 1999, have been swept away by the latest energy

dispute. After Aleksandr Lukashenko's veto put an end to the project of a common monetary and financial system (which had been in the two parliaments' draft constitution since 2003), Russia has now to all intents and purposes dissolved the customs union. The energy conflict reveals that Moscow's alliances are determined no longer by ideological considerations but by market interests, especially when a neighboring state starts pursuing its own interests. Lukashenko, who had called the supply interruption in the gas conflict of 2004 an "act of terror of the highest order," said that the latest developments showed that Russia had now "not only violated the norms of international law, but also destroyed the economic ties that had developed and seriously harmed the prospects of the Belarussian oil refining industry."

The Russian side is also demonstratively turning its back. Whereas in 2000 Putin was still speaking of the "prime importance of strengthening the union" as the "highest form of integration of two states," this time the Russian formulations of "trade war" and "war in the name of the 'Friendship'" demonstrate the fragility of the idea of a "United State of Russia and Belarus." The delegation from Minsk that traveled to Moscow on January 9, 2007, was not even granted a reception. Until recently gestures of such demonstrative contempt would have been as unthinkable as Putin's distancing talk of the "Belarussian colleagues."

By raising gas prices and imposing duty on oil exports to and goods imported from Belarus, Russia has ended the privileged relationship. A further indication that Moscow's course is no longer set for integration is that the most important institution of the "United State of Russia and Belarus," the "Parliamentary Assembly of the Union of Belarus and Russia" was not this time involved in resolving the conflict. Instead, on the Russian side, the Ministry of Economic Development and Foreign Trade of the Russian Federation dealt with the matter. Belarus has become a foreign country. As a measure against vehicle smug-

gling, the Belarussian side is beginning to control Russian citizens crossing the shared border. Temporarily imported vehicles now have to be registered and taxed, although the “Union” rhetoric of 2006 promised to prevent precisely that. The border regime is thus entering a phase of “normalization” whose symbolic ramifications, however, are experienced as alienation. And although the provisional compromise has brought temporary calm, the economic and political conflict can erupt again at any time.

### **Lukashenko’s Existential Crisis**

Even before the crisis broke out it was clear that cheap energy prices were an absolute prerequisite for Lukashenko to maintain his Belarussian model. In recent years Russia has subsidized Belarus on a grand scale. Through cheap energy supplies and re-export of oil products alone, Minsk has earned about \$6,500 million per year. The same sum was lost to the Russian budget. Belarus is heading for a threefold economic crisis.

*Firstly* the Russian gas price increase tears a hole in the state budget. Businesses have to cope with a 50 percent increase in the energy price, which could push especially the large and energy-intensive enterprises over the brink of unprofitability.

*Secondly* Belarus is facing considerable financial losses through falling revenues from oil refining and re-export to EU countries. The state budget could lose around \$4,000 million and the oil refining sector threatens to run into enormous economic difficulties. At Belneftchim, the state-owned enterprise responsible for refining, 125,000 jobs depend directly on oil transport through the “Druzhba” pipeline.

*Thirdly* the situation will be exacerbated still further by the Russian announcement that it intends to impose import duties on Belarussian goods with a total annual volume of around \$6,000 million, starting on February 1, 2007. The duty-free imports granted under the customs union would thus come to an end. Sugar, meat and dairy

products, television sets, and furniture would be worst affected—goods that Belarus sells almost exclusively on the Russian market and whose production depended on cheap energy and a duty-free export market. For example, since the beginning of this year Belarussian sugar can no longer be sold in Russia because Belarus refuses to pay the additional duty. Even though more than half of Belarussian exports now go to countries outside the Confederation of Independent States, above all to the EU, Belarus is still affected by the application of the Russian law on “Special Economic Measures” of December 30, 2006, which permits changes in the customs regime and allows economic sanctions to be imposed on states and organizations. If all three components of crisis came together the regime’s stability would be gone.

The crisis represents a biographical discontinuity for the Belarussian president. Until now Russia was the guiding light of his political life, on which he also aligned the country he governed. The domestic mood in Minsk has become frostier, and external economic pressure is leading the regime’s reactions to become increasingly unpredictable. Lukashenko’s system of power has been weakened both economically and politically. If workers lose their jobs in enterprises that are unable to pay the new energy prices and can no longer sell their goods in Russia due to the imposition of drastic customs levies, or if people begin to freeze, the Belarussians will quickly tire of Lukashenko’s propaganda exhortations to unite behind the regime in a fight on two fronts against Russia and the West and his support will evaporate. In situations like this the sluggish pace of reform of the Belarussian economic system takes its toll. Unprofitable energy-intensive enterprises are directly endangered, while there is but a scattering of small and medium-sized businesses that would be able to respond more flexibly, and the state—as the sole domestic investor—is running out of funds. All this slows down the pace of economic change.

Even after the compromise of January 13, under which Belarus will pay Russian export duties of \$53 per tonne of crude, Lukashenko can no longer count on Russia's unconditional support, especially given that he himself has called into question the security partnership between the two countries. If Minsk were carry out the threat it has occasionally made to demand financial compensation for the Russian military bases in Belarus (which the Russian army currently uses for free) it would have unilaterally terminated the 1998 agreement on the joint use of military infrastructure and in the process completely done away with the "United State of Russia and Belarus." So it comes as no surprise that Russia is showing growing interest in a post-Lukashenko solution. Moscow is developing scenarios to prevent Belarus drifting away westwards under "orange sails" and to open it up for a calculable pro-Russian perspective that the West would be able to accept. Furthermore, Belarus has confirmed its image in Russia as a "risky corridor" and the Kremlin sees an urgent need to think more intensively about ways to reroute energy supplies to avoid Belarus.

Lukashenko responded hectically to the price rise announcements and growing social tensions with personnel changes and policy action in the areas of energy and local government. More hard-liners have been appointed to administer the scarcity of resources and ensure efficient state control. At the same time the regime is preparing for the local elections on January 14, 2007, with its own methods: barring candidates from opposition parties and NGOs, securing exclusive use of administrative resources, filling the electoral commission with loyal civil servants, and preventing election monitoring.

### **Recommendations for EU Policy**

Now more than ever, the EU should raise the pressure on Belarus to modernize, by (a) establishing a permanent EU presence in Minsk, (b) setting up an "Energy Transit"

working party (EU, Belarus, Ukraine, Russia), (c) targeting support to small and medium-sized businesses, alternative energy concepts, and civil society organizations (the German government's "Belarus support program" could act as a pilot project for a wider EU program), and (d) demanding that Belarus sign the Energy Charter Treaty.

Institutionalizing energy relations between the EU and the supplier and transit states is a central task. The EU-Russia energy dialogue and the German-Russian energy dialogue must be conducted more efficiently. Both formats failed in the current transit crisis. The conflict again gives occasion to call for the German-Russian energy dialogue to be opened up to transit countries like Poland, Ukraine, and Belarus. Anyone who is serious about the "strategic partnership" should be urging for energy relations with Moscow and the transit countries to be put on a more solid legal footing.

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