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**BETWEEN THE CO-COMPETITORS:
Belarus, Moldova, Ukraine economic integration in a bi-
polar Europe**

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Abstract

Mind the gap! That is what some authors exclaim when writing about this part of Europe that is located on the border between the EU and Russia. However, representing some 62 million people and 844 thousand square kilometers of land area both Russia and EU would be more than interested to have all countries in the area prosperous. Prosperity means also economic integration that leads to natural economic co-competition between Russia and the EU. This article focuses on the patterns of international economic relations that Belarus, Moldova and Ukraine have with an accent on their economic relations with Russia and the EU. The article summarizes the evidence and concludes with the possible developments in their future economic integration patterns.

Key words: EU's Eastern Neighborhood, Belarus, Moldova, Ukraine, EU-Russia Economic Relations

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1. Introduction

The countries located in the gap between Russia and the European Union are in a difficult position of dealing simultaneously with the gravitational power of both of them. Interestingly for many people in Western Europe the gap is of much undefined essence. In fact even if tempted to exclaim “mind the gap!” in terms of population and land area Belarus, Moldova and Ukraine represent approximately 62 million people and 844 thousand sq. km. Quite a gap! For both Russia and the European Union it would be impossible to create a zone of security and prosperity on their border provided that these three countries stay politically and more importantly economically isolated.

While many studies have been conducted on the political situation in the three countries and the pace and nature of economic reforms taking place in each of them, not much of an analysis is available on the patterns of international economic relations that Belarus, Moldova and Ukraine demonstrate and their likely implications for the future. Of course, to a large extent the foreign economic relations of the three countries are determined by the political and economic interaction in the region that Russia and the European Union build together. As Anatoli Chubais characterizes this interaction will rather have the form of “co-competition” than a partnership (*Chubais, 2004*).

The main objective of this paper is to review the present of their economies and their international economic relations and based on this analysis forecast if the current economic integration of Belarus, Moldova and Ukraine indicates certain direction. The paper does not intend to argue if an economic integration eastwards with Russia or westwards with the EU could be more beneficial but tries to establish which one is more likely to occur.

The paper starts with a very brief description of the political realities in the three countries and then continues with an overview of the economic situation in each of them. Then the paper focuses on the international economic relations patterns in the light of the above mentioned cooperative co-competition between Russia and the European Union. The paper uses mainly literary research and tries to rely on various and independent sources. In some cases using various sources proves the only way to establish some reliable picture of the situation as both statistics and economic reporting could be influenced by politics and in some extreme cases by an outcry propaganda.

2. In unity we differ: political background of Belarus, Moldova and Ukraine

Trying to group and label Belarus, Moldova and Ukraine in one as the EU Eastern neighborhood (or as Russia's Eastern neighborhood) would represent the same mistake as when at the beginning of the 1990s all countries from Slovenia in the West to Lithuania in the East were labeled as Eastern Europe. In fact Belarus, Moldova and Ukraine are quite different in every possible aspect and a serious analysis should start with acknowledging this difference.

If we divide broadly their history in three parts – pre-Soviet history, Soviet times and post-Soviet period we could clearly see that each country in each period have had its own particular path. Formerly part of Romania, Moldova was incorporated into the Soviet Union at the close of World War II. For most of its history Belarus belonged to the Russian empire. Ukraine has the most complicated historic heritage. It was the center of the first Slavic state, Kiev Rus, which during the 10th and 11th centuries was the largest and most powerful state in Europe. Weakened by internecine quarrels and Mongol invasions, Kiev Rus was incorporated into the Grand Duchy of Lithuania and eventually into the Polish-Lithuanian Commonwealth. The cultural and religious legacy of Kiev Rus laid the foundation for Ukrainian nationalism through subsequent centuries. A new Ukrainian state, the Cossack Hetmanate, was established during the mid-17th century after an uprising against the Poles. Despite continuous Muscovite pressure, the Hetmanate managed to remain autonomous for well over 100 years. During the latter part of the 18th century, most Ukrainian ethnographic territory was absorbed by the Russian Empire. Following the collapse of czarist Russia in 1917, Ukraine was able to bring about a short-lived period of independence (1917-20), but was re-conquered and became part of the Soviet Union.

In the Soviet times the three republics also had different experiences. Ukraine was politically and economically the second biggest power in the Soviet Union after the Russian federation. Belarus was also a tangible player in the Soviet reality while Moldova was at the time considered as the rural backyard and its only importance was due to its border for the Soviet Union status.

After the collapse of the Soviet Union the three countries announced their independence but it also had very different and particular features. Although independent from the USSR since 1991, Russian forces have remained on Moldovan territory east of the Dniester River supporting the Slavic majority population, mostly Ukrainians and Russians, who have proclaimed a "Transnistria" republic. Belarus and Russia signed a treaty on a two-state union on 8 December 1999 envisioning

greater political and economic integration. Although Belarus agreed to a framework to carry out the accord, serious implementation has yet to take place.

Ukraine on the other hand is still seeking to find the right political balance between its aspirations to become member of both NATO and the European Union and the necessity to keep a strategic partnership with Russia as there is quite a lot that links the two of them.

Still, politics will be unfortunately of more significant importance than other economic or social factors. So far in the firm hands of a political despot like Aleksandr Lukashenka Belarus might seem politically stable. However no one can guarantee how the country's political landscape could and will look in the post-Lukashenka era when it comes. In the conditions of such unpredictability it is not easy for business to make long term investment decisions.

For Moldova political stability will be established only when and if the Transnistria case is somewhat regulated. Even then it is not sure if the political and the business elite will be able to reach the consensus needed for a coherent and result oriented economic reforms that can elevate Moldova from the poverty. It must be noted that in the case of Moldova Russia is certainly not playing a stabilizing role and it is not clear when and how its attitude will be modified.

Ukraine is a good example. The country is divided between the more pro-Russia orthodox east and the catholic pro-West. So is the political and business elite of the nation. Besides the victory of the supposedly pro-West President Victor Yushenko, one may not ensure that the country is on the path of political stability and healthy democracy.

What could be difficult to speculate is how the EU and particularly Russia will try to influence the future political developments in the region. However the political landscape will to large extent depend on the economic situation in general and particularly on the fact if the local political and business elite finds an economic integration with either East or West more promising.

3. Economic realities and perspectives

In line with the previous paragraph Table 1 could demonstrate that in terms of economic size the 3 countries also differ where Moldova GDP is some 8 times smaller than the Belarus one that is some 4,5 times smaller than Ukraine's GDP. However measured per capita we can observe that Belarus and Ukraine are basically not quite different while Moldova, being among the poorest countries in Europe, has a GDP per capita that is 3 times smaller.

Table 1 Belarus, Moldova, and Ukraine - some economic indicators as of 2003 – 2004

(Source: CIA Fact book, 2005)

Indicator Country	GDP /PPP in US\$/ 	GDP per capita /PPP in US\$/ 	GDP composition by sector	Exports partners	Imports partners
Belarus	70,5 billion	6800	<i>agriculture: 11%</i> <i>industry: 36.4%</i> <i>services: 52.6%</i>	Russia 49.1% UK 9.4% Poland 4.4% Germany 4.2% Netherlands 4.2%	Russia 65.8% Germany 7.1% Ukraine 3.1%
Moldova	8,6 billion	1900	<i>agriculture: 22.4%</i> <i>industry: 24.8%</i> <i>services: 52.8%</i>	Russia 39% Romania 11.4% Italy 10.4% Germany 7.1% Ukraine 7.1% Belarus 5.2% US 4.3%	Ukraine 22% Russia 13% Germany 9.7% Italy 8.3% Romania 7%
Ukraine	299 billion	6300	<i>agriculture: 18%</i> <i>industry: 45.1%</i> <i>services: 36.9%</i>	Russia 17.8% Germany 5.9% Italy 5.3% China 4.1%	Russia 35.9% Germany 9.4% Turkmenistan 7.2%

One question that could serve as a good starting point is why Belarus, Moldova Ukraine failed to match the results that the Baltic States demonstrate at present. The most immediate answer is in the turbulent political life of the former and in somewhat poorly defined and even more poorly implemented reform packages.

3.1. Initial economic shocks after the USSR dissolution

Belarus is a graphic example of the problems created when an "industrial colony" becomes independent. The destructive tendencies caused by disintegration of the USSR, extreme imperfection and low efficiency of a former economic mechanism, have led to worsening of the basic parameters of social and economic development of republic up to the middle of 1990s.

The economic recession in Belarus intensified in 1994, leading to Belarus' worst economic year to that point. In 1994 the GDP dropped by 21 percent from 1993 (down by more than one-third from its 1989 level), which was worse than in the two previous years. Thus in 1995 the GDP went down to a 35% of its 1990 level while industrial output reached 41% and in agriculture as much as to 26%.

Following a civil war in 1992, the region on the left bank of the Nistru River (Transnistria) seceded. Before the breakup, this region accounted for about 40 percent of Soviet Moldova's GDP, 15 percent of its population, and 12.5 percent of its territory. It was also home to the bulk of Moldova's industrial base. Twelve years later, the conflict remains unresolved, largely because there are geopolitical and vested interests in preserving the *status quo*, which provides opportunities for tax evasion, smuggling, and other illegal activities. This situation aggravates Moldova's political risks and hampers growth prospects (*IMF, 2004*).

Moldova promisingly started with its first privatization attempts as early as 1991 with a governmental decree calling for establishment of a market economy but permitting significant provisions for government intervention. The reform was further deepened with a two-part program that aimed to stabilize the economy and provide for the economy's recovery and growth by such means as agrarian and trade reform, social protection, and a legal framework for a market economy. During 1992 enterprise privatization committees inventoried assets at each enterprise in the republic; the aggregate result of this inventory became the basis of calculations of Moldova's total industrial wealth and the following mass privatization. As of the beginning of 1995, Moldova had 4,400 state and 57,000 private enterprises.

At the same time that privatization plans were under way, actual reform efforts were halting and relatively ineffectual, and Moldova's economy declined. A number of factors contributed to the decline, including the complicated political situation in the republic (which had seen several changes of leadership in its first years of existence) and the political and military conflict with Transnistria. The disruption of traditional economic ties with enterprises in Transnistria has had a negative effect on the economy of right-bank Moldova.

After Russia, the Ukrainian republic was far and away the most important economic component of the former Soviet Union, producing about four times the output of the next-ranking republic. Its fertile black soil generated more than one-fourth of Soviet agricultural output, and its farms

provided substantial quantities of meat, milk, grain, and vegetables to other republics. Likewise, its diversified heavy industry supplied the unique equipment (for example, large diameter pipes) and raw materials to industrial and mining sites (vertical drilling apparatus) in other regions of the former USSR.

Shortly after independence in December 1991, the Ukrainian Government liberalized most prices and erected a legal framework for privatization, but widespread resistance to reform within the government and the legislature soon stalled reform efforts and led to some backtracking. Loose monetary policies pushed inflation to hyperinflationary levels in late 1993. Ukraine's dependence on Russia for energy supplies and the lack of significant structural reform have made the Ukrainian economy vulnerable to external shocks. Output by 1999 had fallen to less than 40% of the 1991 level.

3.2. Bottom up

Belarus

After an initial outburst of capitalist reform from 1991-94, including privatization of state enterprises, creation of institutions of private property, and entrepreneurship, Belarus under Lukashenka has greatly slowed its pace of market reforms and privatization, emphasizing the need for a "socially oriented market economy." About 80% of all industry remains in state hands, and foreign investment has been hindered by a climate hostile to business. The banks, which had been privatized after independence, were renationalized under Lukashenka (*D'Amato, 2001*).

President Lukashenka came to power in Belarus on the promises to stop the economic decline and improve living standards and it must be noted that to some extent he delivered. In 1996-2000 GDP went up by 36% and industrial production increased by 65%. The real incomes of the population rose by 71% (*Shimov, 2001*). However, one may argue that the economy remains dependent on Russian subsidies. In 2001 Belarus did receive from Russia the first tranche of a RUB1,5 billion (US\$51,4 million) credit similar to an IMF standby arrangement (*D'Amato 2001*).

Belarus also benefits from importing natural gas at prices that Gazprom uses for the Russian domestic market. The significance of these supplies is shown in Table 2.

Table 2. Natural gas prices Belarus – Ukraine – Poland

(Source: IMF, 2004)

Belarus-Russia: Natural Gas Trade in 2004			
(In millions of US dollars)			
	At 2003 prices	At prices applied to trade with Ukraine	At prices applied to trade with Poland
Natural gas imports (1)	757	900	1206
Gas transit fees paid by Gazprom (2)	90	132	182
Net payment by Belarus (1-2)	668	769	1024
<i>In percent of GDP</i>	<i>3.6</i>	<i>4.1</i>	<i>5.5</i>
<i>In percent of exports</i>	<i>7.1</i>	<i>8.2</i>	<i>10.9</i>
Sources: Belarusian authorities and IMF staff estimates			

The phraseology used by academics includes the “myth of economic revival” (*Marples, 1998*) and the like. One has to be very careful as to determine the truth balancing between the Belarus governmental propaganda and the very limited reliable statistics on which Western criticism is based. Anyway according to Grigory Ioffe economic situation in Belarus is far from serene. Agricultural output is substantially lower than before the Soviet Union’s dissolution, and the inflationary pressure on consumers and the tax burden on enterprises are heavy (*Ioffe, 2004*). Independent Belarus’ economy, like that of the Byelorussian SSR, still relies on inefficient, state-supported, industrial facilities, which are increasingly hampered by their need for fuels whose prices are gradually reaching world levels.

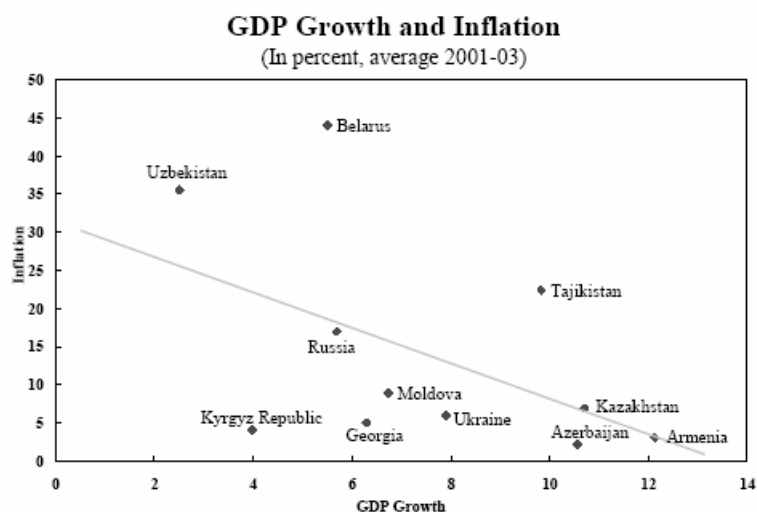
In 2002 Belarus economy remained stagnant or in decline with more than 40% of industrial enterprises operating at a loss. Belarus continued to be heavily dependent on Russia, with the potential for greater economic dependency looming in the proposed EU-style union between the two states. Due to the economic and political climate, little new foreign investment occurred in 2002, while two major companies, the Swedish furniture firm Ikea and Russian beer producer Baltika, ended operations in Belarus due to unrealized government commitments or unwelcome interference.

Major contributors to production growth were rather favorable, on the whole, foreign economic conditions which promoted exports as well as an increase in domestic demand (higher expenditure for final consumption and gross savings). Production of goods and services was increasing with simultaneous reduction in the number of employed which indicates that intensive factors of growth were effective. Productivity (relative to GDP) in 2003 grew by an estimated 8,5% (*NBB, 2003*).

To summarize it **Belarus continues to pursue a gradual approach to economic reforms, hoping in this way to mitigate the social costs of transition.** Recorded real GDP growth was robust during 2003 and 2004 though the staff has growing concerns about the reliability of the official national accounts data. Inflation declined modestly, but remains the highest in the region as shown in Figure 1.

Figure 1. GDP growth and inflation – Belarus, Moldova, Ukraine.

(Source: IMF, 2004)



The authorities, particularly in the presidential administration are reported by the IMF staff to be ambivalent about the need to accelerate structural reforms. The IMF experts point out priority areas for reform to include the energy sector, the business environment, agriculture, labor markets, public administration and public enterprise reform and privatization. Weaknesses in the banking system should also be addressed urgently (*IMF, 2004*).

Moldova

The economic crisis in Moldova could be summarized in brief by Marina Cotruta, an analyst at the EBRD resident office in Moldova saying in 1998 "The country has a debt to GDP ratio of 60%, a severe current account deficit of 13% and a cash fiscal deficit of 7%." (*Gregory, 1998*).

In 1998 after a centre-right government of young reformists was formed it has set about revitalizing the country's stalled reform process, introducing an austerity package and attempting to press ahead with state sales. The government sped an IMF-approved austerity budget through parliament, cutting increases in pensions and state salaries as well as a number of social benefits. Despite its difficult fiscal position, Moldova has managed to achieve some healthy macro-economic fundamentals, including a stable currency and low inflation. After years of experiencing one of the most dramatic falls in GDP in the CIS, peaking at more than 30% in 1994, Moldova started the economic growth, albeit at a modest 1.3% (*Ibid.*). The positive development trends within the main branches of the national economy consolidated in 2002 and GDP registered an increase by 7,2% with some 10,6% increase in industrial output and a 3,0% rise in agricultural output on a year-to-year basis. (*NBM, 2002*).

In 2003 nominal GDP grew further with 6,3% in 2003 while industrial output went up 13,6% as compared to the previous year; real investments went up by 16,0%. However, agricultural output declined by 14,1% in real terms. A problem for the economy remains high rate of inflation of 15,7% recorded at the end of 2003 (*NBM, 2003*). However while economic growth remained high reaching for some 7% in 2004, largely driven by domestic consumption, the economy became increasingly dependent on workers' remittances. Remittances reached almost 25 percent of GDP in 2003 and continued to grow rapidly in 2004, placing Moldova in a clear lead among European countries.

These inflows have helped finance growing imports and fuel short-term growth, while providing a safety net to Moldavians, but they also contributed to strengthening the leu. Despite a large real exchange rate appreciation since mid-2003, external competitiveness appears favorable with exports growing briskly and dollar wages well below those in neighboring countries.

The per capita gross national disposable income marked US\$689 in 2003 as compared to its neighbors, Moldova's post-independence output collapse was deeper and its recovery more sluggish, while human development indicators and per capita foreign direct investment have lagged behind. Moreover, productive capacity has been sapped by the steady exodus of working-age Moldavians following the 1998 crisis (at least 25 percent of the labor force). (*IMF, 2004*)

Ukraine

Upon his election ex-president Leonid Kuchma had pledged to reduce the number of government agencies, streamline the regulatory process, create a legal environment to encourage entrepreneurs, and enact a comprehensive tax overhaul. Results of 2003 confirm that hasty economic growth continues in Ukraine. GDP has augmented by 8,5% while accretion of industrial production constituted 15,8%. Meanwhile GDP increased by 7% and industrial output by 8% in average in the CIS countries (*NBU, 2004*).

Positive dynamics in industry that was the main engine of such development over the whole 2003 was mainly determined by growth of output in machine building, metallurgy, and food industry. Almost three quarters of industrial output accretion were secured by these industries according to the results of 12 months. Improvement of companies' financial and economic activity efficiency on the background of extremely high prices on world markets has led to increase of the share of profitable companies over January – October 2003 to 61% from 57% over the same period of the previous year. Nominal income of profitable companies for this period increased by 15,7% (*Ibid.*).

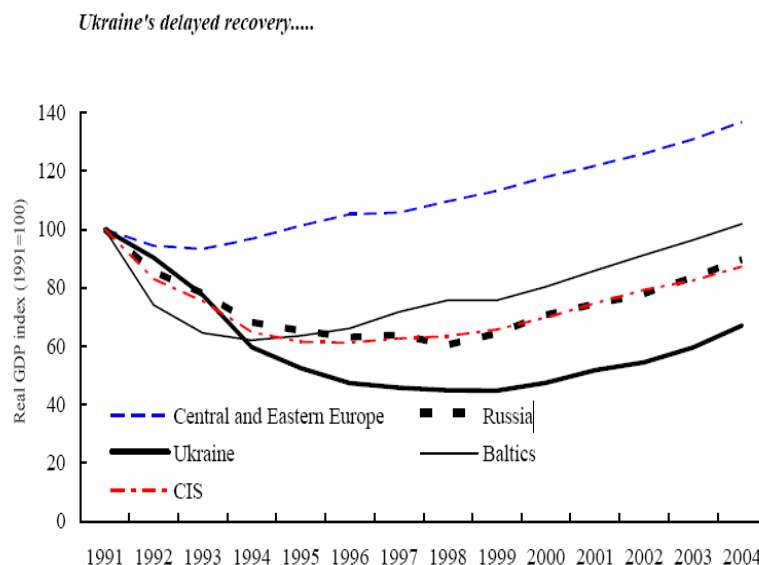
While GDP growth reached 12,7% in 2004 and the current account surplus an impressive 10% of GDP, the loosening of fiscal policy in the second half of the year will exacerbate emerging inflationary pressures. Consumer price index (CPI) inflation is likely to reach 9–10% by year's end, much above the original projection. The discussions took place in the run-up to the October presidential elections, almost certainly a choice between Prime Minister Yanukovich and opposition leader Yushchenko. Irrespective of the results, no major policy change is expected (*IMF, 2005*).

Over 2000-04, GDP growth has averaged 8,4 percent, above the Central and Eastern European average (3,8%), and the Commonwealth Independent States (CIS) average (8,0%), with a projected peak of 12,5% in 2004 (*Ibid.*).

This recovery, however, comes from a low base. Compared with most other transition countries, Ukraine's output contraction in the 1990s was more pronounced as demonstrated in Figure 2. Moreover, delays in structural reforms and a weak business climate have hindered investment. Besides, growth appears not to have benefited everyone in the same proportion.

Figure 2. Real GDP index for Central and Eastern Europe, Ukraine, CIS, Russia and the Baltic States.

(Source: IMF, 2005)



The essence of the Government economic policy in 2004 consists in transition from extensive levers and instruments of economy reforming and state regulation to intensive methods encouraging private initiative. It is expected that accomplishment of such policy would change factors of economic growth from short-term to long range ones (*Ukraine Ministry of Economy, 2004*).

Still, Ukraine remains vulnerable to a sudden reversal in external conditions. Exports account for around 60 percent of GDP, and their buoyant performance over the past couple of years has supported the recovery in domestic demand. Given the surge in private sector debt, a significant drop in external demand could prompt substantial banking losses via the private sector's diminished capacity to repay its domestic debts.

This vulnerability also underscores the need to bring the fiscal deficit down from the level projected for 2004 (3-4%) to prevent a sudden shock from raising it to levels that could make financing problematic (*IMF, 2005*).

From the above presented overview one may see that Ukraine is advancing with its economic reforms but somewhat lacks the speed and the determination of its Eastern European neighbors who already joined the European Union. To its credit it should be noted that its size could be one

explanation. The other is the somewhat more difficult political background that to some extent did not allow for a clear vision and reform objectives.

3.3. Perspectives

Based on the short overview presented above one may conclude that the economies of Belarus, Moldova and Ukraine are still far from being reformed. Privatization, especially in Belarus, is still not concluded while in Moldova and Ukraine it is still half way. The institutional changes in all the three countries needed to make the functioning of market economy possible are too slow the newly devised system is largely dysfunctional. Even if statistics demonstrate some recovery it remains unclear to what extent it is result of healthy economies and to what extent a spill over effect of economic growth in Russia as in the case of Belarus, high demand for commodity exports as in Ukraine or plain dependence on workers' remittances as in Moldova.

The biggest threat is though not in the future of economic reforms themselves as reforms will inevitably continue even if the speed will remain questionable. The threat is twofold. One is the political instability that all the 3 countries still contain and that could have a grave effect on whatever economic achievements and improvements no matter big or small. The second is that the whole political and social structure of the society could collapse because of a rampant corruption. Belarus is listed 73rd, Moldova 112th and Ukraine 122nd in the 2004 Corruption Perception Index 2004. (TI, 2004). In the same table Russia is ranked 90th while closest from the EU countries are Poland 67th and Slovakia 57th.

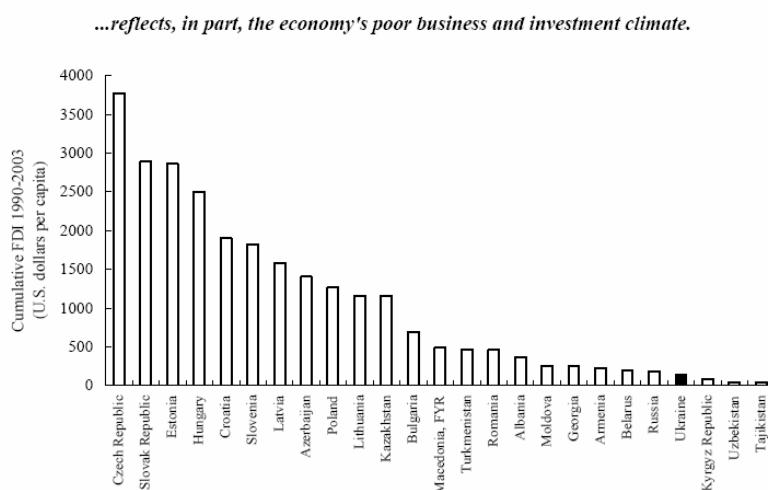
Political instability mixed with corrupt bureaucracies and judicial system is hardly going to create business friendly environment that fosters competition and offers its neighbors opportunities for intensive trade and investments. Therefore for both Russia and the European Union is vital to secure that their neighborhood is a thriving economic space that offers opportunities instead of instabilities.

4. International economic relations: between two too big trade partners

This paragraph should analyze each of the three countries in terms of their foreign trade patterns and Foreign Direct Investments /FDI/ as to speculate and forecast at the end if their future economic integration will be more oriented towards East or West. From the very beginning it must be noted that especially in terms of their ability to attract FDI all the three countries have quite poor record as Figure 3 demonstrates.

Figure 3. Central and Eastern Europe cumulative FDI 1990-2003 in US dollars per capita.

(Source: IMF, 2005)



That will be not surprising provided that for most of the past 15 years all of them failed to create the business environment needed for attracting significant amount of FDI.

4.1. Belarus

Belarus / Foreign trade

By mid-1995 Belarus relied primarily on Russia and other members of the CIS as its primary trade partners but had started looking to expand its economic ties beyond the CIS. It turned to the EU, with whom it signed an agreement with the goal of gradual economic integration of Belarus into the EU, as well as to markets in the east, where it was better able to compete. Although the total volume of Belarus' foreign trade declined by nearly one-third in 1994, the balance of its trade (non-CIS

countries versus CIS countries) improved. Analyzing data of CIS Statistical Committee (Figure 4) we find out that during the 1990s more than half of the Belarus exports and imports are directed to CIS countries.

Figure 4. Belarus exports and imports to CIS versus non CIS countries 1995 – 2004.

(Source: CIS Statistics, 2005)

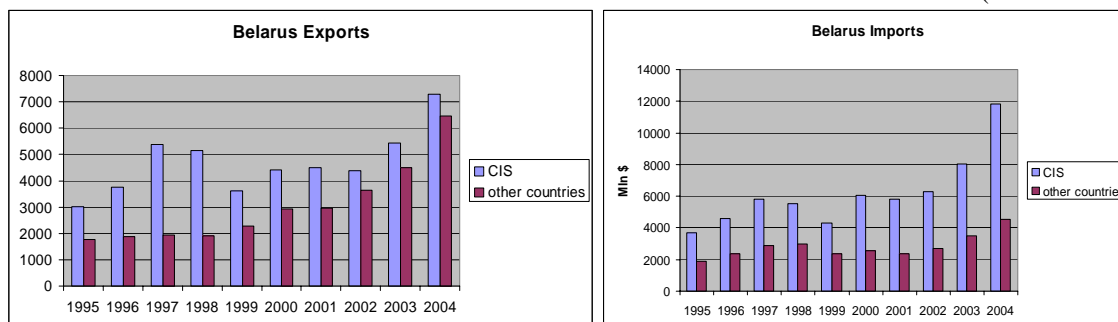


Table 3. Main trading partners of the Republic of Belarus in 2004

(Belarus Ministry of Statistics and Analysis, 2005)

	Mln. US\$	In per cent of total export (import)
Exports		
Russia	6463,0	47,0
Germany	502,9	3,7
Great Britain	1147,6	8,3
Poland	728,8	5,3
Ukraine	539,8	3,9
Netherlands	924,4	6,7
Lithuania	356,3	2,6
China	301,5	2,2
Italy	142,9	1,0
Latvia	326,0	2,4
France	104,6	0,8
USA	162,5	1,2
Brazil	146,4	1,1
Sweden	136,9	1,0
Imports		
Russia	11142,6	68,2
Germany	1081,0	6,6
Great Britain	128,4	0,8
Poland	475,0	2,9
Ukraine	544,9	3,3
Netherlands	118,7	0,7
Lithuania	175,6	1,1
China	158,0	1,0
Italy	300,5	1,8
Latvia	85,0	0,5
France	165,0	1,0
USA	195,1	1,2
Brazil	97,0	0,6
Sweden	98,4	0,6

The volume of trade between Russia and Belarus reached US\$17,5bn in 2004 as Table 3 demonstrates. It is interesting to note that Finland does not reach even 1% of either exports or imports of Belarus. The EU trade with Belarus reached almost €5,3 billion (Table 4) that is almost 3 times less than Belarus trade with Russia.

Table 4. EU-Belarus trade 2000-2004 (in millions of €) (Source: COMEXT, Eurostat)

Year	Imports	Yearly % change	Share of total EU imports	Exports	Yearly % change	Share of total EU exports	Balance	Imports + Exports
2000	1.296		0,13	1.684		0,20	388	2.981
2001	1.358	4,7	0,14	2.017	19,7	0,23	659	3.375
2002	1.537	13,2	0,16	2.089	3,6	0,23	553	3.626
2003	1.972	28,3	0,21	2.218	6,1	0,25	246	4.190
2004	2.660	34,9	0,26	2.627	18,5	0,27	-32	5.287
				2.627	6,2		2.627	2.627
Average annual growth		19,7			11,8			15,4

Export of Belarus is sufficiently various. In the list of export products enter machinery and equipment, mineral products, chemicals, metals; textiles, foodstuffs. This content has been the same during almost the whole considering period. In 2003 mineral products have the main part of export with 23% of the total export, after coming machinery and equipment with 11,4%. According to Central Bank data we find a decreasing tendency for export of machinery and equipment in 2004 with 1% and an increasing one with 3% for mineral products (*NBB, 2002*). The same picture we find for Belarus import. Again main import partners have been CIS, moreover during the last year we find out an increasing tendency for importing goods and services from CIS, mainly from Russia. Structure of import is almost the same as that of export.

Belarus is unique within the CIS in terms of export and import operation. First, Belarus economy is unusually open: in 1999 exports accounted for 55% of GDP (*Muzlova, 2001*). This indicator normally tends to be higher for economically advanced countries of a smaller size (*Hanink, 1996*)

and it is noteworthy that Belarus fits the pattern. Second no other CIS country emphasizes links within the CIS as much as Belarus, as it is shown above. Third, Belarus is second to none in the CIS by per capita value of exports and imports (*Muzlova, 2001*).

Belarus / Foreign Direct Investments

In the Republic of Belarus there are over 3,000 commercial organizations with foreign investments involving investors from over 80 countries. The total amount contributed by foreign investors to the charter funds of such organizations is US\$550 million, of which US\$60 million. Alone was contributed in 2003. Key investing countries are Switzerland, Russia, Great Britain, Germany and USA. Investors from these countries established 1,340 joint and foreign organizations and contributed 90% of all 2003 direct foreign investments to the country's economy (*EoB, 2005*).

In Belarus little FDI derived from the privatization programs. However, privatization programs in Belarus are not likely to attract significant FDI as they are not complemented by market reforms or improvements in the general investment climate. Foreign investors in the republic are attracted by industry. Industry, and in particular food, light industry and chemistry, as well as engineering and metal processing, in 2003 received over 60% of the total contributions to the charter capital. Over 16% of direct investors' capital is used to finance development of trade in the republic. Transportation receives about 10% of contributions to charter funds (*Ibid.*).

Joint ventures with foreign participation and foreign companies make a significant contribution to the development of the Belarus economy. They provide employment for up to 10% of the working population of the republic and account for 10% of the country's GDP. Joint and foreign companies participate actively in the country's international trade through exporting over 15% of the total export volume and importing about 20% of the total import volume (*MinEcon, 2004*).

Foreign capital is also invested into the banking sector of the Republic of Belarus: 25 out of 30 banks are established with the participation of foreign capital. German “Kommerzbank AG”, Polish “Bank Polska Kasa Opieki”, Russian “Inkombank” and “Mestbank” are among 11 offices of foreign banks, credit and financial organizations operating on the territory of the Republic of Belarus.

Above 10 insurance companies with the participation of foreign capital operate on the insurance market of Belarus. 70% of direct investments account for industry, 46,8% of thereof – for food

industry, 11,6% - for machine building, metal working, 8,7% - for light, 8,5% chemical, 8,5% - for wood working, 6,3% - for medical. 17,5% account for trade and public catering, 4,5% - for transportation (*export.by, 2005*).

Still, as of 1998 there were only five firms in Belarus with capital of over US\$10m. These included JV Coca Cola - Amatil Belarussia (US\$59,9m), JV Dynamo-programme (US\$14,7m), JV Frebor (US\$14,4m), JV Rautaruukki Belcolor (US\$13,7m), and JV Civil Project (US\$10,5m). Approximately 60 companies recorded a statutory capital declared by the foreign partner from US\$1m to US\$10m (*Ugorich 2002*).

By the beginning of 2003 the Russian investments in Belarus represented approx. 45% of the all cumulative investments. The share could be even bigger as Russians often invest also via companies registered in offshore zones and /or countries in Western Europe. (*Godin, 2004*). It is also Russians that founded the largest number of Joint Ventures or fully Russian owned companies in Belarus as indicated in table 5.

Table 5. Biggest investors in terms of registered companies as of January 2004.

(Source: *export.by, 2005*)

Russia	579 or 19,5% from the total number of registered companies
USA	419 or 14,2% from the total number of registered companies
Germany	341 or 11,5% from the total number of registered companies
Poland	322 or 11,5% from the total number of registered companies),
Lithuania	205 or 6,9% from the total number of registered companies
UK	147 or 4,9% from the total number of registered companies
Latvia	138 or 4,7% from the total number of registered companies
Cyprus	124 or 4,2% from the total number of registered companies
Czech republic	92 or 3,1% from the total number of registered companies
Italy	77 or 2,6% from the total number of registered companies

4.2. Moldova

Moldova / Foreign Trade

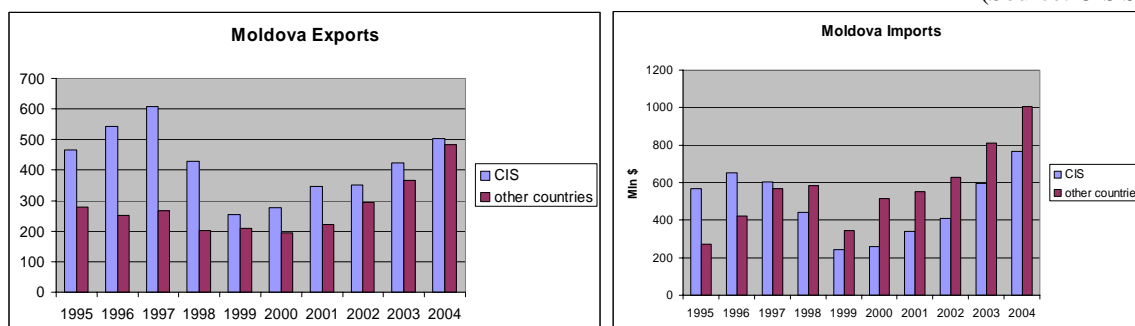
Within the Soviet economy, Moldova was an importer of industrial raw materials, fossil fuels, and manufactured goods. Its primary exports to other Soviet republics included wine and spirits, processed foods, clothing and textiles, and small amounts of electrical equipment.

Since independence, Moldova has struggled to reorganize its domestic economy and at the same time to reorient its foreign trade, finding new markets for its products and new sources for the essential imports it traditionally obtained from the Soviet Union. In 1991, however, 73 percent of Moldova's imports and 96% of its exports were still directed toward territories of the former Soviet Union. By 1994 73% of Moldova's foreign trade was with other members of the CIS, and only 27% was with the West. In 1994 exports totaled US\$580 million and imports totaled US\$662 million.

In 2003 both exports and imports of goods recorded higher values and the imports grew by 37,6% while exports grew by 22,2%. 84,5% of exports were directed towards Moldova's traditional trade partners: Russia (39,0%); Romania (11,4%); Italy (10,4%); Ukraine (7,1%); Germany (7,1%); Belarus (5,2%); the USA (4,3%). Exports over 2003 were mainly supported by five items of exported goods, which made up 77,2% of total value (*NBM, 2003*). Figure 5 shows the dynamics in the structure of Moldova exports and imports.

Figure 5. Moldova exports and imports to and from CIS versus non CIS countries 1995 – 2004.

(Source: *CIS Statistics, 2005*)



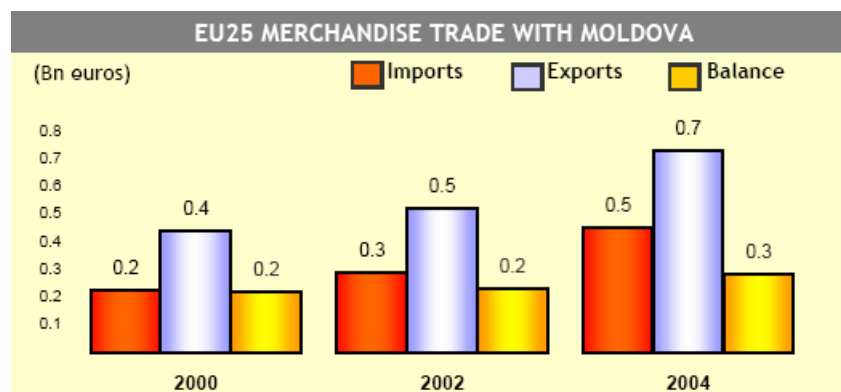
Imported energy resources in 2003 amounted to US\$232,83 million, surpassing by 19.9% the value of 2002. The majority of these imports came from Ukraine – 41,4%; Russia – 36,0%; Romania – 11,4% and Belarus – by 7,5%. The material value of imported coal increased by 78,2% from the previous year; of natural gas – by 8,1%, of diesel – by 14,3%, of gasoline – by 20,8%; at the same time imported fuel oil reduced by 1,0% (*NBM 2003*).

The EU is Moldova's most important trading partner with a share of 36% in total bilateral trade. Bilateral trade with the EU was €1 billion in 2003 and €1,2 billion in 2004 as presented in Figure 6. In 2003 33,8% of Moldovan exports went to the EU and 37,1% of imports were from the EU.

Moldova mainly exports agricultural and food products, textiles, and base metals and articles. Its main imports from the EU are machinery and electrical products, agricultural products and textiles. In recent years, Moldova has repeatedly run trade deficits, both overall and with the EU (€0,3 billion in 2003). Its trade structure remains oriented towards the CIS. (EU, 2005).

Figure 6. EU25 merchandise trade with Moldova in 2000, 2002 and 2004.

(Source: Eurostat, 2005)



The trade with Russia for the first 6 months of 2004 including statistics from Transnistria region reached US\$373,8 that was an increase of 26,3% compared to 2003 where the Moldova exports to Russia were US\$202,6 million and its imports accounting for US\$171,2 million. The trade structure stayed unchanged. Moldova exports to Russia spirits, wines and canned foods. Russia exports to Moldova primarily fuels. Based on these data Russia represents 35,2% of the Moldova exports and 12,6% of the Moldova imports (Interlic, 2004).

Moldova / Foreign Direct Investments

Until 1998, foreign investment in Moldova indicated a steadily increasing trend. It slowed in late 1998-1999 due to the severe impact in Moldova of the Russian economic crisis. Foreign investment recovered near the end of 2000. According to National Bank of Moldova (NBM) data, 2001 foreign direct investment (FDI) inflows to Moldova amounted to US\$131,26 million.

According to the National bank of Moldova the annual FDI inflows to Moldova were as indicated in table 6.

Table 6. FDI in Moldova 1996-1997 (in million USD)(Source: *NBM*, 2003)

<u>1996</u>	<u>1997</u>	<u>1998</u>	<u>1999</u>	<u>2000</u>	<u>2001</u>
23,18	78,29	76,25	40,35	142,69	148,51

Note: All data on FDI excludes Transnistria

By the end of 2001, the total FDI stock in Moldova amounted to some US\$608 million, including foreign investment companies' charter capital of some US\$477 million.

To the end of year 2001, according the statistical department data, their 2402 enterprises with foreign capital registered, 808 of them are 100% foreign capital formation and 1594 on bilateral and multilateral base. According to the Department of Statistics, FDI stocks by country of origin for the ten largest investing countries were (as of January 2002) Russia 149, Spain 46, USA 39; Germany 17, France 17, Great Britain 16; Liechtenstein 11, Canada 10, Greece 8 Ireland 8 (*BSEC*, 2002).

According to the Russian Ambassador in Moldova Nikolai Ryabov the Russian investments in the country reached US\$170 million and account for 40% of all investments (*Ryabov*, 2004).

Foreign direct investment has been largely confined to the agricultural and food processing sectors, with a small proportion in a handful of the country's high-yielding commercial banks. The EBRD and World Bank are among the most active investors in the country. There have also been significant capital inflows from Russia, Romania and Greece. The main reasons cited by the government for lack of foreign investment have been political instability created by the civil war with secessionist Transnistria and a general lack of awareness of potential opportunities. The major obstacle cited by foreign investors who have considered the country for their portfolio has been a lack of attractive stock.

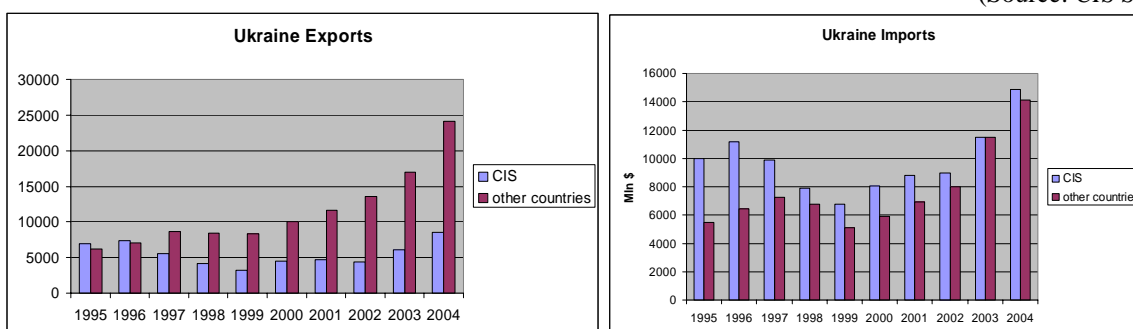
4.2. Ukraine

Ukraine / Foreign Trade

Analyzing data of the department of statistics of CIS one can understand that after 1997 Ukraine exports to non CIS countries more than twice exceeds exports to CIS countries as it is shown in Figure 7. The situation with import to Ukraine is a bit more diversified as we find in the early 90-s more import from CIS and particularly from Russia and nowadays we can see a balance in absolute values of import to Ukraine (CIS).

Figure 7. Ukraine exports and imports to and from CIS versus non CIS countries 1995 – 2004.

(Source: *CIS Statistics, 2005*)



In 2003, the growth rates of exports and imports of goods and services were the highest, making 124 and 128,7% respectively against the background of a considerable surplus of the BOP current account. The exact volumes and structure of Ukrainian exports and imports is presented in Table 7.

An augmentation of the volumes of exports did not considerably change their breakdown. As previously, two thirds of the exports' growth fell on the products with low level of processing delivered to the international markets i.e. products of metallurgy and chemical industries, and of fuel and energy complex as well. Within the total exports, the share of machine building products went up from 14,1% in 2002 to 15,3% in 2003 (*NBU, 2004*).

In 2003, the growth rates of exports of machine building products made 138,3% versus 112,4% in 2002. The largest amount of machine building products was exported to CIS countries. Nevertheless, the share of exports to these countries reduced from 53,4 to 46,4% of the total exports of this group. At the same time, the share of European countries went up from 25,6 to 36,5% (*Ibid.*).

More than a third of the total exports fell on metallurgy industry products, though within the total exports, the share of this group diminished from 38,2% in 2002 to 35,8% in 2003. On the whole over the year, exports of ferrous metals in terms of value augmented by 25,4% chiefly at the expense of a rise in prices (on average by 30 - 35%) and increase in the share of products with a relatively high level of processing (*Ibid.*).

Table 7. Geographical structure of Ukrainian exports and Imports (US\$ million)

(Source: *National Bank of Ukraine, 2004*)

	Total	CIS countries	Other countries of the world*)	Europe	EU countries	Asia	Africa	America	Australia and Oceania	Unspecified countries
Export										
1996	14400,8	7405,2	6995,6	3456,9	1596,4	2711,0	209,3	598,3	20,1	-
1997	14231,9	5585,7	8646,2	3675,3	1757,1	3829,2	472,4	652,5	16,8	-
1998	12637,4	4202,3	8435,1	3993,0	2119,3	2997,0	562,0	865,4	17,4	0,3
1999	11581,6	3252,2	8329,4	3790,2	2118,6	3183,8	617,1	692,4	45,1	-
2000	14572,5	4497,5	10075,0	4680,2	2354,4	3437,9	731,5	1217,5	7,0	0,0
2001	16264,7	4675,4	11589,3	5720,9	2976,5	3970,2	877,0	1011,9	7,4	-
2002	17957,1	4377,4	13579,7	6515,8	3530,0	5067,7	1055,2	936,9	4,1	-
2003	23066,8	6044,4	17022,4	9147,4	4559,3	5400,7	1250,3	1219,2	4,8	-
Import										
1996	17603,4	11175,9	6427,5	4655,6	2769,0	668,8	141,5	931,0	24,3	-
1997	17128,0	9879,4	7248,6	5451,6	3379,3	837,2	136,8	797,9	22,0	-
1998	14675,6	7897,0	6778,6	4998,5	3170,5	879,1	118,7	755,5	20,9	5,2
1999	11846,1	6743,2	5102,9	3547,4	2398,9	756,7	157,8	588,4	27,2	25,4
2000	13956,0	8039,9	5916,1	4311,5	2881,2	832,0	136,4	581,4	54,7	0,1
2001	15775,1	8832,2	6942,9	4981,7	3422,0	970,8	198,5	740,9	51,0	-
2002	16976,8	8968,2	8008,6	5751,1	507,6	1171,6	177,3	856,7	51,5	0,4
2003	23020,1	11508,5	11511,6	8165,6	5800,2	1971,2	248,8	1072,2	53,4	-

Exports of fuel and energy complex products grew the most dynamically. Within the total exports, the share of this group increased from 11,2% in 2002 to 13,9% in 2003 due to high growth rates of exports of these products (157,8%). Exports of oil products in terms of value multiplied 1,3 times chiefly at the expense of a rise in prices (by 25% on average). At the same time, exports of gas and oil in terms of value increased 3,3 and 4,3 times respectively (*Ibid.*).

In 2003, imports of machines, equipment and modes of transportation multiplied 1,5 times (32% of the total growth). Energy carriers increased 1,2 times in terms of value (23,2% of the total growth), while agricultural products grew twice in terms of value (17,5% of the total growth). As a result, in 2003, imports of goods augmented (*Ibid.*).

Within the total imports, the share of fuel and energy complex products diminished from 38,6 to 34,7%. Nevertheless, within the breakdown of Ukrainian imports, energy carriers prevail, which shows that Ukrainian economy (including export-oriented branches viz. chemical and metallurgical industries) greatly depends on external deliveries of energy carriers.

During 2003, the volumes of imported oil for processing at petroleum refineries grew by 19%, amounting to 22,5 million tons. The value of the imported oil multiplied 1,5 times chiefly due to 27% rise in average annual prices (*Ibid.*).

The enlarged EU has replaced Russia as Ukraine's foremost commercial partner (accounting for 32,5% of its external trade in 2003). Both the EU and Ukraine are therefore interested in maintaining and strengthening solid, predictable, transparent and open trade relations. In 2004, Ukraine's total trade with the 25 countries of the EU amounted to around €17,6 billion, a figure which has been growing steadily since the economic crisis in 1998. However, Ukraine's manufacturing and trade structures are unbalanced. Energy and agricultural products accounted for around 32% of the Ukrainian exports to the EU, whilst machinery and chemical products appear prominently in EU exports to Ukraine. EU-Ukraine trade in services is very limited in value terms, below €1,5 billion in 2003, and the level of foreign investment in Ukraine also remains low (*EU, 2005*).

EU imports from Ukraine are to a very large extent liberalized. The only exception is trade in certain steel sector products, which is currently governed by autonomous measures to be replaced by an agreement, the negotiations of which were completed on 31 March 2005. This new agreement will provide for a quota of 908 000 tones in 2005 and for a quota of 1 004 500 tones in 2006 for imports from Ukraine (*Ibid.*).

As a trade partner Russia alone is not lagging far behind. Based on data from statistics and the customs committee of Ukraine, in 2004 the bilateral trade volume between the two reached US\$17,7 billion that was some impressive 36,6% more than in 2003. The Ukrainian exports amounted for US\$5,9 billion while imports reached US\$11,8 billion leaving a trade deficit of US\$1,6 billion. It is interesting to observe that only in 5 years (199-2004) the bilateral trade more than doubled with Ukrainian exports going up 2,5 times while imports rising 2,1 times (*UkEmb, 2005*).

The 2004 Ukrainian exports to Russia consisted of machinery and equipment, metallurgy, food and chemistry. The imports not surprisingly dominated by raw materials: fuels 63,4%, metallurgy 6,9% and chemicals 6,0% as well as machinery 14,9% (*Ibid.*).

Ukraine / Foreign Direct Investments

Table 8 shows the inflows of FDI in Ukraine for the period 1995-2004.

Table 8. Ukraine inwards and outwards FDI 1995 - 2004

(Source: *Ukrainian Committee of Statistics*)

	Foreign direct investment in Ukraine	Direct Ukrainian investment abroad
01.01.1995	483,5	20,3
01.01.1996	896,9	84,1
01.01.1997	1438,2	97,4
01.01.1998	2063,6	127,5
01.01.1999	2810,7	97,5
01.01.2000	3281,8	98,5
01.01.2001	3875,0	170,3
01.01.2002	4555,3	155,7
01.01.2003	5471,8	144,3
01.01.2004	6794,4	166,0
01.01.2005	8353,9	175,9

Studying investment in Ukraine, both Ukrainian and foreign experts have noticed a paradox: being potentially attractive for investors, possessing a great amount of physical and human capital, large domestic market with 48 million people, and easy access to large markets of Russia and other FSU countries, Ukraine is not succeeding well with attracting investors(*Tiusanen et al., 2004*).

Most investors are attracted to Ukraine's domestic market of 48 million people. The availability of low-cost labor turned out to be insignificant for the majority of companies surveyed except entrepreneurial investors, who tend to be more sensitive to the availability of cheap inputs. Although Ukrainian wages are lower than in other Eastern-European countries, this competitive advantage is diminished by significantly lower labor productivity, the lack of capital, inferior management and regulatory burdens. Thus unit costs in Ukraine are not necessarily much cheaper than in neighboring countries (*Flemings/SARS survey 2000*).

Ukraine has got FDI from 114 countries. The USA holds the first place among countries investing in Ukraine. Table 9 shows the FDI coming from the EU by country.

Table 9. Direct foreign investment in Ukraine by EU country

(Source: *Ukrainian Committee of Statistics*)

	Volume of direct investment as of	
	01.01.2004	01.01.2005
EU countries, total	3805,3	4652,4
Austria	252,5	345636,58
Belgium	27,9	42,7
Greece	14,9	164,4
Denmark	73,8	106,3
Estonia	16,5	25,8
Ireland	77,3	54,7
Spain	36,0	38,6
Italy	94,9	106,1
Cyprus	901,2	1035,6
Latvia	71,9	32,7
Lithuania	32,0	28,8
Luxembourg	40,9	58,5
Malta	7,7	8,2
Netherlands	459,9	548,3
Germany	451,6	631,6
Poland	152,7	192,3
Portugal	2,1	2,284
Slovakia	46,0	45,8
Slovenia	3,5	3,6
United Kingdom	701,2	895,9
Hungary	128,7	179,1
Finland	6,4	7,7
France	59,2	79,1
Czech Republic	42,7	46,3
Sweden	103,1	120,3
For information:		
Ukraine, total	6794,4	8353,9

Russia invested US\$378 million in the Ukrainian economy in 1999-2003, the Ukrainian State Statistics Committee told RBC. Over this period, Ukraine received US\$1,1 billion in investments from the United States, \$779 million from Cyprus and \$686 million from the UK (*Gateway Russia, 2004*).

As for the Russian investments in Ukraine according to the Ukrainian ambassador in Russia Nikolay Beloblockii at the end of 2001 the cumulative amount represented US\$4,1 billion (*MDOOffice, 2001*). However it is very difficult to establish the exact volume of Russian investments as for instance according to various experts Russian and Ukrainian capital often goes through Cypriot and British offshore centers. That also explains partially the impressive figures for the two countries in table 9.

5. Conclusions

Belarus, Moldova and Ukraine would continue to be in the delicate position of being simultaneously the Russian and the EU neighborhood. In this process it comes only naturally that Russia and the EU countries will have an economic and to a lesser extent political co-competition for the markets of these countries.

In this co-competition each of the two powers will have its own leverages to increase its overall influence. Based on the presented above analysis these leverages could be summarized in the following table:

Table 10. Russian leverages for economic and political influence on Belarus, Moldova and Ukraine

Leverages Country	ECONOMIC					POLITICAL		
	Imports	Exports	Investments	Economic assistance	Energy resources			
	Russia EU	Russia EU	Russia EU	Russia EU	Russia EU	Russia EU	Russia EU	
Belarus	US\$11,1 billion €2,6 billion	US\$6,46 billion €2,7 billion	45% of all cumulative investments	US\$175 million €22 million (1991-2004)	supplied at preferential prices	Ever closer political union Untold possibility to become EU member	Withdrawing support for President Lukashenka Attractiveness of the EU economic and social model	
Moldova	12,6% of total 37,1% of total	35,2% of total 33,8% of total	40% of total n/a	None €197 million	supplied at preferential prices	Moldovan workers in Russia Untold possibility to become EU member	Transnistria The attractiveness of the EU economic and social model	
Ukraine	US\$11,8 billion €5,8 billion	US\$6,9 billion €4,6 billion	Cumulative US\$4,1 billion (end of 2001) cumulative €4,7 billion	None €38 million (1991 – 2004)	supplied at preferential prices	Ukrainian workers in Russia Untold possibility to become EU member	Russian citizens in Ukraine The attractiveness of the EU economic and social model	

If table 10 shows that to some extent the score in the co-competition between EU and Russia is almost even, the future tendencies could be hard to monitor and predict. One reason is that the political developments could be to some extent predictable only in the biggest country – Ukraine. What will be the solution of the Transnistria conflict in Moldova and when and how is Alexandr Lukashenka going to step down could be only guessed and that makes it hard for investors to estimate the political risks. In terms of their international economic relations or in short term and near term future one threat and two tendencies could be identified and forecasted.

Trade deficits

The main threat is that Belarus, Moldova and Ukraine could fall in the trap of serious trade deficits as they will be in need of importing fuels and energy from Russia and growing imports from the EU countries. By IMF estimates Staff estimates that an oil price increase of US\$10 per barrel would raise Moldova's trade deficit by 2,5 percent of GDP and consumer prices by 2–2,5% (*IMF, 2005*). According to Gazprom Deputy CEO Alexander Ryazanov "Moldova gas industry is well able to work according to market principles and from 2006 gas supplies to Moldova may be carried out at market prices, which correspond to European (prices)" (*Pravda.ru, 2005*).

Following the December 2004 elections in Ukraine Russia's Gazprom bullied Ukraine by proposing to raise prices for its gas exports to Ukraine to US\$160 per 1,000 cubic meters from the currently US\$55 paid by Naftogaz Ukraine (*MosNews, 2005*). It is difficult to estimate what will be the precise effect if prices triple since 2006.

The total transit tonnage of 193 million tones in 1999 between the European Union and Russia was distributed among transport corridors as follows: Ukraine– Slovakia 72 million tones, Belarus– Poland 46 million tones, Latvia 42 million tones, Estonia 20 million tones, Lithuania 10 million tones, and Finland 3 million tones. Transit fees are an important source of revenues, not only for the Baltic countries, but for Ukraine as well. Ukraine imports 88 million tones of gas a year and obtains 40% of its own gas consumption in transit fees (*Laurila, 2003*).

Raising prices for fuels and energy together with a growing demand for Western capital goods and products will inevitably put a considerable strength on the macroeconomic stability of Belarus,

Moldova and Ukraine. One way to avoid this risk is in a dramatic increase in the amount of FDI attracted. It is precisely in the FDI where two major tendencies could be highlighted.

An increased outward expansion of Russian corporations

The growing international expansion of Russian companies has been well documented (*Liuhto 2001; Liuhto&Jumpponen, 2001, 2003; Vahtra&Liuhto, 2004*) and is certainly gaining momentum. For Russian corporations Belarus, Moldova and Ukraine represent a natural interest as they are in geographic proximity, speak Russian and provide interesting investment opportunities. As the Russian Financial and Industrial Groups /FIG/ are in their best ever financial shape they pay and should pay bigger attention to the business potential of the Russian neighborhood. Lukoil, Tatneft, Vimpelcom, Rusal, Baltica are just some of the known names that have serious interests in the three countries. The Russian investors have also a clear advantage as unlike their Western competitors they are less afraid of institutional instability, corruption and generally unfriendly business environment.

Western investors awaiting improvements in business climate

Nevertheless as the three countries improve their general business climate they will have bigger chances to attract also Western investments. As Moldova is too small and poor and Belarus is politically quite far from the EU vision for a democracy, Ukraine has the biggest chances for attracting significant amount of FDI from the EU. Interestingly it is also Ukraine that could experience biggest problems with its trade deficits and consequently its macroeconomic stability. Still as shown in Figure 3 there is along way until Ukraine reaches the FDI per capita of Poland.

Would these FDI come from Russia or from the EU will make quite a difference for the future economic and perhaps political integration of Ukraine and to some extent of the region. The answer is rather in the hands of the Ukrainian policy makers than in the good will of the EU.

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