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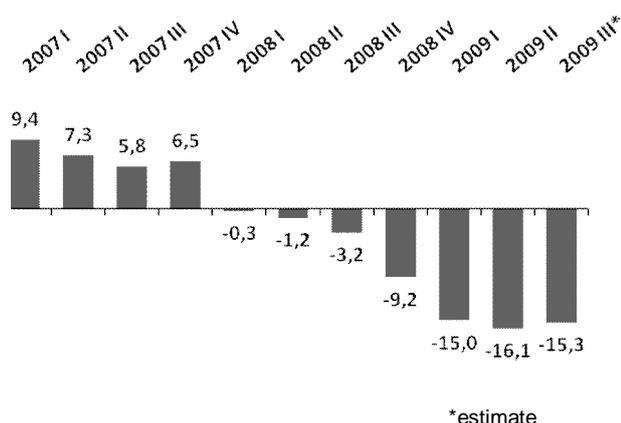
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Estonia

Decrease in the GDP decelerated

According to the preliminary estimates of Statistics Estonia, the Estonian GDP decreased by 15.3% during the third quarter of 2009 compared to the corresponding period of the previous year. This is slightly less than the decrease during the second quarter, when the GDP dropped by 16.1%.

Real growth rate of GDP by quarters in 2007Q1–2009Q3 (y-o-y, %)



Source: Statistics Estonia

Both the weak domestic and external demand continued to influence the Estonian GDP during the third quarter of 2009. The GDP has now remained negative for seven quarters, although the decrease slowed down during the Q3.

Fall in industrial production slowed down

According to Statistics Estonia, the production of industrial enterprises in October decreased by 20.9% y-o-y.

The production in manufacturing dropped by 21.9% in October 2009 compared to the corresponding month of the previous year. The decline was mainly due to insufficient demand both in domestic and external markets. Production decreased in almost all manufacturing sub-sectors. Particularly bad figures were noted in the manufacturing of chemicals and chemical products (-38.5%), fabricated metal products (-35.0%), building materials (-32.4%), and electrical equipment (-31.2%). Growth was recorded in only three sub-sectors, the manufacturing of beverages, textiles and other transport equipment, of which the manufacturing of beverages grew the most, by 19.9%.

The total energy production in Estonia in October 2009 decreased by 19.5% compared to the corresponding month of 2008, of which the production of electricity declined by 33.0% and the production of heat increased by 17.0%. Electricity production fell due to a partial replacement of locally based production in Estonia with imports from Lithuania.

Estonia - main economic indicators	2001	2002	2003	2004	2005	2006	2007	2008	2009	as of
GDP (y-o-y %-growth, constant prices)	6.5	8.0	7.2	8.3	10.2	11.2	7.1	-9.7	-15.3	Q3/2009
Industrial production (y-o-y %-growth)	8.9	8.2	11.0	10.5	11.0	7.3	6.1	-6.5	-20.9	10/2009
Inflation (CPI, end of period, y-o-y %-change)	4.2	3.6	1.3	3.0	4.1	4.4	9.6	10.4	-2.1	11/2009
General government budget balance (% of GDP)	0.3	1.5	2.0	2.3	2.3	3.8	2.8	-3.0	n/a	1-12/2008
Gross wage (period average, EUR)	352	393	430	466	555	596	784	838	752	Q3/2009
Unemployment (% end of period)	11.9	11.3	9.3	8.5	7.9	5.9	4.7	5.5	14.6	Q3/2009
Exports (EUR million, current prices)	3698	3642	4003	4770	6190	7647	8028	8454	4713	1-9/2009
Imports (EUR million, current prices)	4798	5079	5715	6704	8213	10576	11278	10872	5395	1-9/2009
FDI inflow (EUR million, current prices)	603	307	822	775	2255	1341	1817	1366	188	1-6/2009
Current account (% of GDP)	-5.6	-10.6	-11.6	-12.5	-10.5	-14.8	-17.4	-9.2	4.9	Q2/2009

Sources: Statistics Estonia, Bank of Estonia, author's calculations

Declining trend in the construction market

The total production of Estonian construction enterprises fell by 29.0% during the third quarter of 2009, compared to the corresponding period of the previous year, Statistics Estonia reports. The production value of construction enterprises amounted to EEK 6.4 billion (EUR 409 million). The stable decline has continued during this year – in the first quarter of 2009 the production decreased by 31.0% and in the second quarter by 28.0% y-o-y. The decreased volumes in dwelling construction on the domestic construction market were the main reason for the decline. The volume of building construction at constant prices declined by approximately a third, totaling EEK 3.7 billion (EUR 236 million), and the volume of civil engineering by approximately a fourth, totaling EEK 2.7 billion (EUR 173 million).

Decrease in the consumer price index

The consumer price index in November 2009 decreased by 2.1% compared to November 2008, Statistics Estonia reports. With regard to the different commodity groups, the prices for housing dropped the most, by 7.0% y-o-y. Price decreases were also recorded in food and non-alcoholic beverages (-6.8%), hotels, cafés and restaurants (-3.1%), and recreation and culture (-1.9%). In turn, the prices for health rose by 2.3%, education by 1.8%, transport by 1.2%, household goods by 1.0%, communications by 0.6%, clothing and footwear by 0.4%, and alcoholic beverages and tobacco by 0.3%.

Change of the consumer price index in selected commodity groups in November 2009 (%)

Commodity group	y-o-y	Previous month
Food and non-alcoholic beverages	-6.8	-0.3
Clothing and footwear	0.4	-0.1
Housing	-7.0	-0.4
Transport	1.2	0.4
Hotels, cafés and restaurants	-3.1	-0.3
TOTAL	-2.1	-0.2

Source: Statistics Estonia

Some business highlights

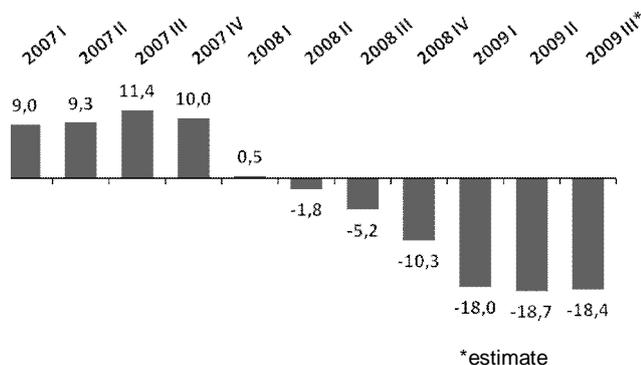
- The Estonian government will buy the country's power-grid operator Elering for EEK 2.7 billion (EUR 173 million) from Eesti Energia. The agreement was made due to EU regulations that demand the separation of the ownership of grids from electricity production and sales, the Estonian government says.
- The real-estate prices in Tallinn have decreased by approximately a half from the spring 2007 when prices reached their peak. The value of the private house market in Tallinn and Harju county, on the other hand, has fallen by 50% in a year. Especially hard to sell are new housing estates outside the city borders, which have experienced the biggest drop in prices.

Latvia

Deep recession continues in Q3

According to the preliminary estimates of the Central Statistical Bureau of Latvia, the Latvian GDP decreased by 18.4% during the third quarter of 2009 compared to the corresponding period of 2008.

Real growth rate of GDP by quarters in 2007Q1–2009Q3 (y-o-y, %)



Source: Central Statistical Bureau of Latvia

According to the Bank of Latvia's analysis, the future growth of the Latvian economy will depend on both external and domestic developments, mainly the durability of the economic recovery trend in the U.S. and in Europe and the restored confidence in the stability of Latvia's economy. The economic forecasts project a slightly lower decrease in the Latvian GDP than was previously forecasted – a 17.0% to 17.5% decrease in 2009 and a 2.0% to 2.5% decrease in 2010.

Industrial production still declining

Industrial production output in October 2009 declined by 13.5% compared to October 2008, the Central Statistical Bureau of Latvia reports. Manufacturing decreased by 15.8%, mining and quarrying by 11.0%, but electricity and gas supply only by 2.0%.

With regard to the manufacturing sub-sectors, the most notable decreases were recorded in the manufacturing of motor vehicles, trailers and semi-trailers (-53.2%), other non-metallic mineral products (-52.1%), wearing apparel (-49.7%), fabricated metal products, except machinery and equipment (-41.7%), machinery, mechanisms and equipment (-41.5%), and other transport equipment such as building of ships and boats, manufacture of railway locomotives and rolling stock (-41.5%). On the other hand, growth was recorded in the manufacturing of basic metals (up by 26.0%), wood and cork articles, except furniture (up by 20.2%) and chemicals and chemical products (up by 6.2%).

Construction volume went down

Construction in Latvia during the third quarter of 2009

Latvia - main economic indicators	2001	2002	2003	2004	2005	2006	2007	2008	2009	as of
GDP (y-o-y %-growth, constant prices)	8.0	6.5	7.2	8.5	10.6	12.2	10.3	-10.3	-18.4	Q3/2009
Industrial production (y-o-y %-growth)	6.9	5.8	6.5	6.0	5.6	4.8	0.5	-6.7	-13.5	10/2009
Inflation (CPI, end of period, y-o-y %-change)	3.2	1.4	3.6	7.3	7.0	6.8	14.1	15.4	-0.9	10/2009
General government budget balance (% of GDP)	-2.1	-2.3	-1.6	-1.0	-0.4	-0.2	0.0	-4.0	n/a	1-12/2008
Gross wage (period average, EUR)	282	297	298	314	350	430	683	678	644	Q3/2009
Unemployment (% end of period)	12.9	11.6	10.3	10.3	8.7	6.8	5.4	9.9	18.4	Q3/2009
Exports (EUR million, current prices)	2232	2416	2559	3204	4085	4594	5727	6202	3568	1-9/2009
Imports (EUR million, current prices)	3910	4284	4634	5671	6879	8828	10986	10534	4792	1-9/2009
FDI inflow (EUR million, current prices)	n/a	223	248	489	568	1324	1797	909	89	1-9/2009
Current account (% of GDP)	-7.6	-6.6	-8.1	-12.9	-12.3	-21.1	-22.8	-12.6	14.2	Q2/2009

Sources: Central Statistical Bureau of Latvia, Bank of Latvia, author's calculations

contracted by 36.8% y-o-y, the Central Statistical Bureau of Latvia reports. The volume of building construction decreased by 53.3% and the volume of civil engineering structures by 19.5%. The construction volume at current prices during the third quarter amounted LVL 288.1 million (EUR 407.1 million).

The most notable decreases were seen in the construction and repair of production buildings and warehouses (-78.5%), wholesale and retail trade buildings (-76.0%), residential buildings (-73.1%), office buildings (-60.3%), hotels and similar buildings (-55.5%), and motorways and streets (-42.9%). In turn, the public construction in Latvia appears to have increased. The construction of health care and social care buildings grew by 45.7%, local pipelines and cable lines by 28.8% and ports and dams by 24.5%.

Inflation decreased in October

According to the Central Statistical Bureau of Latvia, the consumer price index decreased by 0.9% in October 2009 compared to October 2008. The prices for clothing and footwear decreased by 8.4%, housing, water, electricity, gas and fuels by 5.4%, food by 5.3%, transport by 5.1%, hotels and public catering by 4.8%, communication by 2.0%, and furnishing, household equipment and operation by 1.8%. On the other hand, price increases were recorded in alcoholic beverages and tobacco (20.8%), health care (17.8%), education (10.4%), and recreation and culture (1.1%).

Change of the consumer price index in selected commodity groups in October 2009 (%)

Commodity group	y-o-y	Previous month
Food	-5.3	0.2
Clothing and footwear	-8.4	1.5
Housing, water, electricity, gas, fuels	-5.4	-0.4
Transport	-5.1	-1.5
Hotels and public catering	-4.8	-0.6
TOTAL	-0.9	-0.2

Source: Central Statistical Bureau of Latvia

Some business highlights

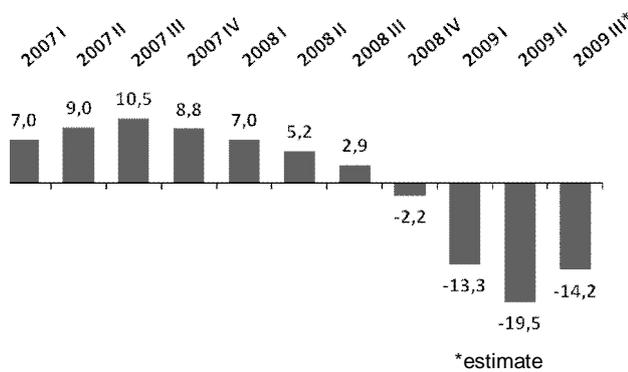
- The Latvian energy company Latvenergo has signed a contract with Energijos Realizacijos Centras (ERC), a subsidiary of Inter RAO JES, to supply electricity to Latvia. In view of its contracts with Russian and Belarusian energy suppliers, ERC could deliver up to 7 TWh of electricity to the Baltic Countries in 2010.
- Ventspils Nafta, a Latvian oil tranship company, has reported a sharp loss in profits. Company's nine months profit went down from LVL 14 million (EUR 20 million) to LVL 0.7 million (EUR 1.0 million) in a year. According to company representatives, Ventspils Nafta's performance has been affected by the economic crisis and global market competition.

Lithuania

Some improvement in the economy

According to the second estimate of Statistics Lithuania, the Lithuanian GDP decreased by 14.2% during the third quarter of 2009 compared to the corresponding period of 2008. According to Bank of Lithuania, the data shows that the Lithuanian economy has reached its turning point and started to recover. However, the Bank of Lithuania points out that the other macroeconomic indicators don't yet support the recovery of the Lithuanian economy and therefore the improvement in GDP should be estimated cautiously. The Bank of Lithuania forecasts that the Lithuanian GDP will decrease by 15.2% in 2009 and 1.5% in 2010.

Real growth rate of GDP by quarters in 2007Q1–2009Q3 (y-o-y, %)



Source: Statistics Lithuania

Based on the provisional data of Statistics Lithuania, almost all business activities and non-market services made negative results during the third quarter of 2009. The biggest decreases in the value added were recorded in construction (45.0%), trade, transport and communication (15.7%), industry and energy (15.1%), and financial intermediation, real estate and other business (12.4%). The value added of public administration and defence, education, health care and social work activities decreased slightly, by 1.2%. Only the value added of agricultural enterprises increased, by 4.9%.

Youth unemployment still growing rapidly

The unemployment rate in Lithuania reached 13.8% in the third quarter of 2009, Statistics Lithuania reports. The unemployment rate grew slightly, by 0.2 percentage points, compared to the previous quarter. Compared to the same quarter of the previous year, the unemployment rate in Q3 2009 was 2.3 times higher.

The youth (aged 15–24) unemployment rate has reached an alarming level, 33.3%, in the third quarter of 2009. The number of young unemployed persons has doubled in a year, from 26 000 to 53 000 people.

Lithuania - main economic indicators	2001	2002	2003	2004	2005	2006	2007	2008	2009	as of
GDP (y-o-y %-growth, constant prices)	6.6	6.9	10.3	7.3	7.9	7.8	8.9	3.0	-14.2	Q3/2009
Industrial production (y-o-y %-growth)	16.0	3.1	16.1	10.8	7.3	8.9	7.2	2.7	-8.8	10/2009
Inflation (CPI, end of period, y-o-y %-change)	2.0	-1.0	-1.3	2.9	3.0	3.8	8.1	10.9	1.3	10/2009
General government budget balance (% of GDP)	-2.0	-1.4	-1.3	-1.5	-0.5	-0.3	-1.2	-3.2	n/a	1-12/2008
Gross wage (period average, EUR)	274	293	311	335	421	459	594	672	620	Q3/2009
Unemployment (% end of period)	17.4	13.8	12.4	11.4	8.3	5.6	4.3	5.8	13.8	Q3/2009
Exports (EUR million, current prices)	4778	5526	6158	7478	9502	11250	12522	16074	8469	1-9/2009
Imports (EUR million, current prices)	6767	7943	8526	9959	12446	15384	14341	21026	9555	1-9/2009
FDI inflow (EUR million, current prices)	516	772	160	623	826	1448	1645	1223	426	1-6/2009
Current account (% of GDP)	-4.7	-5.1	-6.8	-7.7	-7.2	-10.8	-13.7	-11.6	-0.2	Q2/2009

Sources: Statistics Lithuania, Bank of Lithuania, author's calculations

Sharp decline in construction output

According to Statistics Lithuania, the volume of construction work carried out by Lithuanian enterprises during the third quarter of 2009 plummeted by 48.5% compared to the corresponding period of the previous year. Building construction fell by 58.0% and construction of civil engineering structures by 38.6% y-o-y. The total value of the construction work amounted LTL 1663 million (EUR 482 million) at current prices, of which 97.4% was accomplished within Lithuania and 2.6% was accomplished abroad. New construction made up 38.2% of the total value of the construction work carried out within Lithuania and amounted LTL 618 million (EUR 179 million).

Annual inflation increases

The consumer price index in October 2009 increased by 1.3% compared to the corresponding month of 2008, Statistics Lithuania reports. The growth in inflation rate was mostly influenced by the price rises of alcoholic beverages and tobacco products (up by 19.1%), and health care (up by 15.6%), as well as the price decreases of clothing and footwear (down by 9.9%) and food products and non-alcoholic beverages (down by 3.3%).

Compared to September 2009, the consumer price index in October went down by 0.4%.

Change of the consumer price index in selected commodity groups in October 2009 (%)

Commodity group	y-o-y	Previous month
Food and non-alcoholic beverages	-3.3	-0.5
Clothing and footwear	-9.9	1.9
Housing, water, electricity, gas etc.	0.1	-4.7
Transport	-1.4	-0.3
Hotels, cafés and restaurants	2.0	-0.1
TOTAL	1.3	-0.4

Source: Statistics Lithuania

Some business highlights

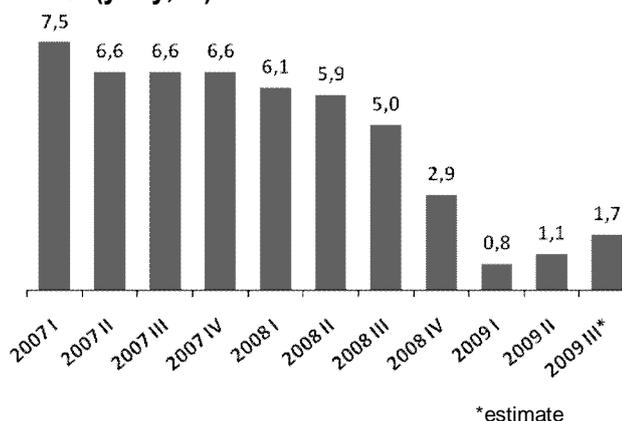
- The British bank Barclays will open an information technology centre in Vilnius, Lithuania. The centre, which will be fully operational by mid-2010, is expected to employ around 250 people by the end of 2011. Barclays is the third largest bank in the U.K. and currently has three similar information technology centres around the world.

Poland

Small growth in GDP continues

According to the preliminary data of the Central Statistical Office of Poland, the Polish GDP continued to grow slightly during the third quarter of 2009, by 1.7%, compared to the corresponding period of the previous year. The economic growth was mainly supported by net exports and consumption.

Real growth rate of GDP by quarters in 2007Q1–2009Q3 (y-o-y, %)



Source: Central Statistical Office of Poland

According to the National Bank of Poland, the recent macroeconomic data on Poland suggests that the economy might start to slowly recover. However, the situation in the labour market, the rising unemployment rate in particular, remains of concern. According to the Central Statistical Office of Poland, the unemployment rate in October 2009 reached 11.1%. It has been growing slightly during recent months and is 2.3 percentage points higher than in the corresponding month of the previous year.

Slight decrease in industrial output

According to the Central Statistical Office of Poland, industrial output in October fell by 1.2% compared to the corresponding month of the previous year. Industrial output decreased in 19 out of 34 industrial sectors. With regard to the main industrial sectors, mining and quarrying declined the most, by 11.1% compared to the corresponding month of the previous year. Manufacturing decreased slightly by 1.1%. In turn, the output in the other two main industrial sectors increased – electricity, gas, steam and air conditioning supply went up by 1.9% and water supply, sewage treatment, waste disposal and land rehabilitation by 0.6%.

Among the manufacturing sub-sectors the sharpest decline in output in October was recorded in other transport equipment (-39.2%). A double-digit decrease was also registered in machinery and equipment, which fell by 17.7%. In turn, the computers, electronic and optical products sub-

sector grew the most rapidly, by 13.9% y-o-y. Paper and paper products (up by 9.5%) and beverages (up by 7.8%) increased as well.

Annual inflation at 3.1%

According to the data of the Central Statistical Office of Poland, the consumer price index in October increased by 3.1% compared to the corresponding month of the previous year. With regard to the different commodity groups, the most notable increases were recorded in alcoholic beverages and tobacco (up by 8.9%), housing, water, electricity and other fuels (up by 6.7%), dwelling (up by 5.7%), restaurants and hotels (up by 4.4%), and healthcare (up by 3.3%). In turn, the prices for clothing and footwear decreased by 6.3%, transport by 0.7% and communication by 0.3%.

Compared to the previous month, the consumer price index in October 2009 increased by 0.3%.

Change of the consumer price index in selected commodity groups in October 2009 (%)

Commodity group	y-o-y	Previous month
Food and non-alcoholic beverages	3.0	0.3
Clothing and footwear	-6.3	1.7
Dwelling	5.7	0.2
Transport	-0.7	-0.8
Restaurants and hotels	4.4	0.2
TOTAL	3.1	0.1

Source Central Statistical Office of Poland

Some business highlights

- The U.S.-based information technology giant IBM is opening two IT centres in Poland. The first one, a Business Innovation Center in Krakow, has already started operating in October. One of the main purposes of the centre is to provide Polish companies with expertise concerning the use of new technology solutions. The other one, an Integrated Delivery Center located in Wroclaw, is planned to be operational by the spring 2010. The centre will help to deliver IT services to European customers. It is expected to employ approximately 2000 people.
- The Swedish furniture giant Ikea will build a shopping centre in Swicza, Poland. The value of the project is approximately PLN 500 million (EUR 123 million). Besides the Ikea store, the 110 000m² shopping complex will host several other retail outlets, and is expected to employ around 2500 people.
- Kronospan company plans to invest PLN 414 million (EUR 100 million) to expand its factory in Strzelce Opolskie, Poland. Kronospan is one of the world's leading producers of wood-based panels.
- The German Messer group will invest over PLN 124 million (EUR 30 million) to open a production plant for liquid gases in Rybnik, southern Poland.

Poland - main economic indicators	2001	2002	2003	2004	2005	2006	2007	2008	2009	as of
GDP (y-o-y %-growth, constant prices)	1.1	1.4	3.8	5.3	3.5	6.2	6.7	4.8	1.7	Q3/2009
Industrial production (y-o-y %-growth)	0.6	1.1	8.3	12.6	4.1	5.7	9.7	3.5	-1.2	10/2009
Inflation (CPI, end of period, y-o-y %-change)	3.6	0.8	1.7	4.4	0.7	1.4	4.0	4.2	3.1	10/2009
General government budget balance (% of GDP)	-3.7	-3.3	-2.9	-3.3	-6.1	-3.9	-1.9	-3.9	n/a	1-12/2008
Gross wage (period average, EUR)	557	544	497	505	591	692	825	821	758	Q3/2009
Unemployment (% end of period)	18.5	19.7	19.3	18.0	16.7	12.2	11.4	9.5	11.1	10/2009
Exports (EUR billion, current prices)	40.4	43.4	47.5	59.7	71.4	87.5	101.1	114.6	70.0	1-9/2009
Imports (EUR billion, current prices)	56.2	58.3	60.4	71.4	80.6	100.0	118.8	139.3	76.4	1-9/2009
FDI inflow (EUR billion, current prices)	6.4	4.4	3.7	10.0	8.3	15.1	12.8	11.1	4.8	1-9/2009
Current account (% of GDP)	-2.9	-2.6	-2.1	-3.5	-1.7	-2.3	-3.7	-5.4	-0.6	H1/2009

Sources: Central Statistical Office of Poland, National Bank of Poland, author's calculations

St. Petersburg

Economy: possibly at bottom

August-October 2008 turned to be a three-month period of economic resurgence both in Russia in general and in St. Petersburg in particular. This might be both a start of recovery, and a temporary correction of a downward trend. The deepest fall of regional industry was observed in July 2009, when its output was 40.0% less than a year before. In September 2009 the corresponding decline accounted for 22.1%, y-o-y, and in October 2009 the industrial sector of St. Petersburg lost 20.7% of its production value compared to the corresponding month of 2008. Thus, the volatility of the crisis lowered, creating a certain stability, and giving some ground for preliminary evaluations. During the first ten months of 2009 almost all sectors of the regional economy contracted significantly: construction down by 26.6%; industry by 23.2%; catering by 18.0%; retail trade by 10.0%; consumer services by 9.0%, y-o-y. Investment in non-financial assets decreased in January-October by 24.7%, y-o-y. Price-driven 4.9% y-o-y growth of monetary output of regional transport came along with a 15.4% y-o-y decline of the sector's physical output, measured by tonnes of carried cargoes. Communication's slight y-o-y increase of 2.8% in January-October 2009 was also a result of raising tariffs. To conclude these results, the region's economy stopped its downward slide, but the magnitude of this ten-month reduction was much higher than anywhere in Russia's North-West. To compare, the aggregated industrial output of North-West Federal District in October 2009 was only 9.3% lower than a year before. In some of North-West regions, namely in Vologda Province and in Nenets Autonomous District, industrial output even grew in October 2009, y-o-y, marking the end of recession in that basic sector of their economies.

Foreign investment: changed structure

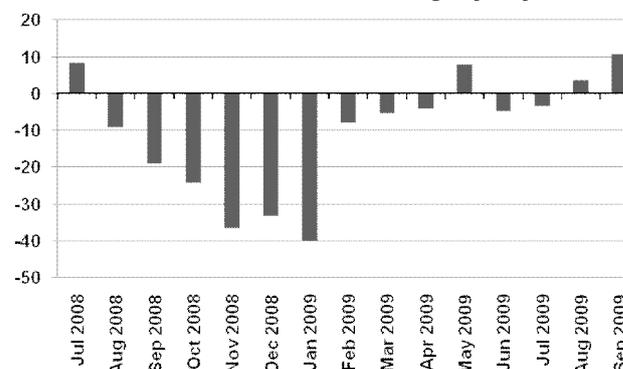
Foreign investment dynamics in St. Petersburg were in line with general trends of the region's economy: total non-financial investment from abroad in January-September 2009 decreased by 36.6%, y-o-y. Nevertheless, the structure of foreign investment has changed significantly within the first three quarters of 2009. In the pre-crisis period the bulk of money coming to St. Petersburg was classified as *other investment*, which came in the form of short- and long-term loans. These investment flows originated from global financial centres and offshore countries. In these new economic conditions other investment suffered most: its volumes contracted in January-September 2009 by 48.9%, y-o-y. Contrary to this, FDI went up by 4.2%, y-o-y. Another beneficiary of the first three quarters of 2009 was the sector of portfolio investment. It increased fivefold, up to RUB 3.86 billion (EUR 87.7 million). More than 90% of this investment came from USA, as US-based global funds were utilising huge bailout resources through investment in emerging markets. The share of portfolio investment reached 4.3% of the total, while FDI was responsible for 30.3% of capital inflow from abroad, compared to 18.4% for FDI in January-September 2008. The country structure of FDI to St. Petersburg's economy changed as well: Finland became the leading source of direct investment with a total sum of RUB 11.85 billion (EUR 269.5 million). The share of Finland in total

FDI inflow into the region was 39.9%; second position was occupied by Germany with 15.7% of total FDI value.

Private incomes: resurgence

Real incomes of St. Petersburg's residents were the first victim of the economic crisis, starting to fall sharply even prior to the major downturn in economy: a significant reduction in earnings already started in August 2008.

Real incomes of residents, % change, y-o-y



Source: Petrostat, 2009

The deepest fall of real incomes since October 2008 until January 2009, when this indicator lost almost 40% compared to a year before, was the result of decreasing nominal earnings combined with the high inflation rate. However, since mid-summer 2009 both trends changed: nominal incomes started to revive, and inflation fell. In fact, the price rise in the first quarter of 2009 was, to a large extent, a consequence of the rouble's devaluation. The last wave of rouble's strengthening against foreign currencies (i.e., the basket of US dollar and euro) in August-October 2009 pushed inflation down, and CPI shifted to a negative zone. The deflation of these three months is still less than one percent, but it was enough to increase real incomes in the region. Another reason for improvement in field of private incomes was the state raising pensions; real pensions in St. Petersburg grew 8.6% in October 2009, y-o-y.

Some business highlights

- St. Petersburg's biggest machine-builder, namely Silovye Mashiny, reported a significant growth of its net earnings in January-September 2009: RUB 3.87 billion (EUR 88.0 million) compared to RUB 277 million (EUR 6.3 million) in the corresponding period of 2008. The reason was an increasing portfolio of new orders, both from Russian and foreign partners. To develop its success, the machine-builder announced plans for expanding the company's product line of power generators for nuclear power stations. Creation of production facilities, needed for building new types of generators, will require investment of RUB 5.94 billion (EUR 135 million) during a period until December 2013.
- Gazprom, Russia's biggest energy holding, acquired 17.7% share of TGK-1, the biggest energy generator of Russian North-West in addition to 28.7% of TGK-1's stock already owned by the gas giant, thus becoming a key player in regional power generation. Revenues of TGK-1 in the first half of 2009 grew 20.9%, y-o-y.
- St. Petersburg State University of Telecommunications launched its new technological centre named IKT-1251. Investors in the project were companies from the innovation sector, namely Digiton, Easy Technologies, Nokia Siemens Networks; their investment accounted for RUB 329.9 million (EUR 7.5 million).

St Petersburg - main economic indicators	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	as of
GRP of St Petersburg (y-o-y %-growth, constant prices)	10.5	4.5	17.7	8.4	7.2	8.4	8.4	9.1	8.7	n/a	1-12/2008
Industrial production (y-o-y %-growth)	26.2	0.2	31.4	5.8	14.1	4.2	-7.0	10.0	4.1	-23.2	1-10/2009
Regional inflation (CPI, y-o-y %-change)	23.5	16.3	16.6	13.0	12.7	12.0	10.0	10.9	14.9	13.6	1-10/2009
Gross average wage (monthly, EUR)	n/a	n/a	217	209	285	344	407	510	667	537	9/2009
Unemployment (% average annual)	7.9	4.4	3.5	4.3	2.8	2.4	2.4	2.0	2.0	4.0	1-10/2009
Exports (EUR million, current prices)	2736	2134	1839	2428	3210	3953	5499	12978	16055	6997	Q1-Q3/2009
Imports (EUR million, current prices)	2693	4423	5158	5123	5560	8081	10299	15093	17475	8689	Q1-Q3/2009
FDI inflow (EUR million, current prices)	158	127	89	62	90	200	512	567	581	675	Q1-Q3/2009

Source: Petrostat, Rosstat, Central Bank of Russia, European Central Bank, author's calculations

In 2002 and 2004 average wage is for December; in 2003, 2005, 2006, 2007 and 2008 wage is for November of corresponding year

Leningrad region

Economy: recovery continues

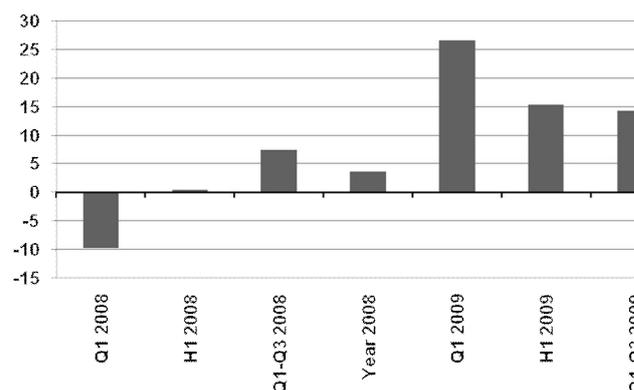
The economy of Leningrad province continued to recover from its deepest fall since the late 1990-ies. The core sector of the region's economy, namely industrial production, experienced stabilisation in August-October 2009, being on average 3.8% lower than in August-October 2008. This was a significant recovery, as in May 2009 y-o-y reduction of regional industrial output was at its maximum of 15.3%. In general, during the first ten month of the crisis year of 2009 the industry lost 7.0% of its output, y-o-y. Moreover, even the relatively favourable level of January-October 2009 remains largely affected by the problems of the industry's biggest outsider, namely the automobile branch: during this period production of transport machine-builders contracted by 36.7%, y-o-y. The falling production of cars, however, was in line with the global downward trend in this field. At the same time food production, the biggest branch of the regional industrial sector, experienced a 4.5% y-o-y growth in January-October 2009. Zero y-o-y change was observed in petroleum processing, as consumer demand for gasoline remained almost stable throughout the reviewed period of 2009. A certain fall in construction activity in the beginning of 2009 was compensated for by a huge increase in the autumn months of the year: in October alone construction went up 29.7% y-o-y. As a result, the total value of the construction sector's output in January-October 2009 was 3.0% higher than in the corresponding period of 2008. Transport and communication continued to increase in August-October 2009; for the whole period since January 2009 these sectors went up by 23.5% and 10.2% y-o-y, respectively. Whilst some part of the increasing value output of these two sectors relates to raising tariffs, another part of the surplus appeared due to higher volumes. For example, the cargo turnover of regional transport companies in January-October grew 4.6%, with the largest contribution being pipeline transporters. The service sector remained in reduction phase mostly due to real incomes of the residents which continued to fall, in October 2009 by 2.1%, y-o-y. Retail trade was down 4.7% in October 2009, while for the first ten months of 2009 its total contraction stood at 2.1%, y-o-y. Consumer services were in January-October 2009 just 0.7% lower than a year before. Some worsening was observed in October 2009 in the region's agricultural sector: its monthly output dropped down by 13.3%, y-o-y. However, from January-October 2009 the total results of agricultural producers remained in the positive area, being 1.6% higher than a year before. This sudden drop might be a consequence of increasing food imports which rose due to the rouble's strengthening: in October 2009 Russia's national currency reached its highest levels against the euro and US dollar since late 2008.

Investment: good performance

Investment in non-financial assets in Leningrad province in January-September 2009 grew 14.3% y-o-y; their amount totalled RUB 123.1 billion (EUR 2.8 billion). The bulk of this investment came into three sectors of the regional economy: transport and communication having 43.1% of the total

inflow; production of energy, gas and water with 21.8%; and manufacturing with 20.9%. In fact, the investment targets of Leningrad province were sectors linked with infrastructure, transportation and industrial production. Shares of construction and real estate in the first three quarters of 2009 decreased compared to the corresponding period of 2008: 0.7% in comparison to 2.1%; and 3.3% to 5.5%, respectively. Thus, speculation-driven investment was replaced by production-driven money flows.

Investment in non-financial assets, y-o-y change, %



Source: Petrostat, 2008, 2009

Foreign trade: still falling

Foreign trade of Leningrad province continued to fall in the second and the third quarters of 2009, losing 51.9% of its total value, y-o-y. Imports remained low, especially in a segment of non-food products and durables: the total reduction of imports in January-September 2009 was 61.4%, y-o-y. Exports showed better performance due to increasing prices on mineral fuel; its share in the total exports of the region was 82.4%. Commodity structure of regional imports changed in favour of food products, their share in the total value of imported goods reached 29.3%.

Some business highlights

- On November 11, 2009, Finland and Sweden granted permits to EU-Russian pipeline operator Nord Stream AG to utilise their marine exclusive economic zones for building the gas line, connecting Vyborg, Leningrad province, and Germany's Greifswald. For the pipeline project, this fact meant the end of the long-lasting procedure of planning and harmonisation, and the start of construction itself.
- Kingisepp Dairy Plant, one of the biggest manufacturers of dairy products in Leningrad province, announced its plans for creating an agricultural cooperative with a large number of dairy farms in the region. A closer unification of different segments of the production chain might enable the dairy plant to expand production and secure its supplies of milk. The examples of foreign competitors such as Valio or Campina prove this scheme to be economically effective.
- Finnish Nokia Tyres launched a new residential complex called Hakkapeliitta Village near Vsevolozhsk, Leningrad province. Apartments in the new complex could be acquired only by personnel of Nokia Tyres' subsidiary in Vsevolozhsk. Affordable mortgage programmes were also offered by the Finnish company to the potential buyers of 167 new apartments.

Leningrad region - main economic indicators	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	as of
GRP of Leningrad Province (y-o-y %-growth, constant prices)	12.8	8.5	16.3	14.6	8.8	8.3	8.1	8.5	7.6	n/a	1-12/2008
Industrial production (y-o-y %-growth)	26.8	10.7	35.6	20.9	10.3	5.9	26.9	2.6	1.0	-7.0	1-10/2009
Regional inflation (CPI, y-o-y %-change)	23.5	19.6	14.8	13.0	14.9	12.0	9.9	9.3	15.5	14.7	1-10/2009
Gross average wage (monthly, EUR)	105	141	152	173	190	259	324	403	492	427	9/2009
Unemployment (% average annual)	12.7	10.8	9.6	9.2	7.5	7.8	6.2	3.3	3.2	8.9	1-10/2009
Exports (EUR million, current prices)	1786	2350	2301	2580	3886	4862	5443	6078	7870	3815	Q1-Q3/2009
Imports (EUR million, current prices)	328	810	939	1061	1372	2562	2858	4759	5932	1958	Q1-Q3/2009
FDI inflow (EUR million, current prices)	222	266	122	104	107	179	288	277	258	133	Q1-Q3/2009

Source: Petrostat, Rosstat, Central Bank of Russia, European Central Bank, author's calculations. In 2000-2008 average wage is for November of corresponding year

Kaliningrad region

Modest growth in recent months

In the last three-four months Kaliningrad's economy seems to be on the path of a modest recovery driven mainly by improving external economic conditions. Manufacturing output has been growing since June on the month-on-month basis. Continued appreciation of the rouble should improve demand in Russia for goods manufactured by Kaliningrad's import-processing sector. Real disposable household incomes have also continued to grow and in January-September they were slightly higher (by 0.1%) than a year ago. Retail sales increased in September and October year-on-year. The number of registered unemployed dropped in September-October. The net financial results of large and medium-sized enterprises moved into positive territory in August.

But recovery has been weak and fragile so far, and major downside risks remain. For example, investment in fixed assets was 31% lower in the first nine months of 2009 than a year ago and this decline accelerated in the third quarter. The construction sector is still contracting and credit availability remains limited.

Growth rates by sectors, y-o-y, %

	1-10/2009	1-10/2008
Industrial production	-11.8	4.6
Extraction industries	-4.9	-0.7
Manufacturing	-23.0	10.4
Electricity, gas and water	-7.7	4.6
Construction	-9.5	45.7
Retail trade	-1.2	19.2

Source: Kaliningradstat (2008-2009)

Foreign investment inflows dry up

The global economic crisis has undermined the willingness of foreign investors to take on new ventures. After the boom in inward foreign investment in 2007-2008, in the first nine months of 2009 inflows dropped by 71%.

Inward foreign investment, million EUR

	1-9/2009	1-9/2008
FDI	26.0	91.9
Portfolio investment	3.7	22.6
Trade loans	7.6	11.6
Other loans	23.6	81.2
Other investment	0.2	1.4
Total	61.2	208.9

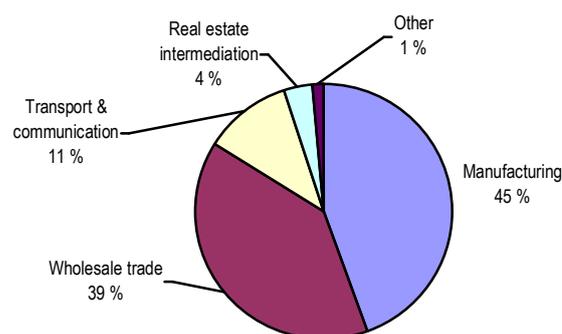
Source: Kaliningradstat (2008-2009)

Many foreign investors have decided to leave both Kaliningrad's and the Russian market altogether. Such examples include a large Brazilian meat processor Sadia SA, a Lithuanian refrigerator manufacturer Snaige, a British consumer finance company International Personal Finance plc, etc.

Kaliningrad region - main economic indicators	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	as of
Regional GDP (y-o-y %-growth, constant prices)	15.1	3.2	9.5	9.3	12.6	3.6	15.3	19.9	9.7	n/a	1-12/2008
Industrial production (y-o-y %-growth)	32.4	12.9	4.2	4.7	22.5	27.4	66.6	34.8	2.5	-11.8	1-10/2009
Inflation (CPI, end of period, y-o-y %-change)	17.5	21	9.8	17.5	11.7	11.1	7.9	11.2	15.2	9.3	10/2009
Gross wage (period average, EUR)	67	99	125	137	155	193	285	358	430	364	9/2009
Unemployment (% end of period, LFS data)	15.6	10.6	7.2	7.6	6.5	6.6	4.5	3.4	8.7	11.6	Q2/2009
Exports (EUR million, current prices)	514	508	497	507	876	1 470	2 025	3 666	765	95	Q1/2009
Imports (EUR million, current prices)	947	1 169	1 701	1 894	2 419	3 283	4 275	5 714	6 564	841	Q1/2010
Exports (sales) to Russia (EUR million, current prices)	459	691	802	989	1 449	1 901	2 471	3 901	3 805	n/a	1-12/2008
FDI inflow (EUR million, current prices)	7.1	3.6	6.3	12.4	18.0	15.1	16.9	117.9	109.4	26.0	1-9/2009

Source: Kaliningrad Statistical Office, RosStat, Central Bank of Russia, author's calculations

FDI Inflow by Sector, January–September 2009

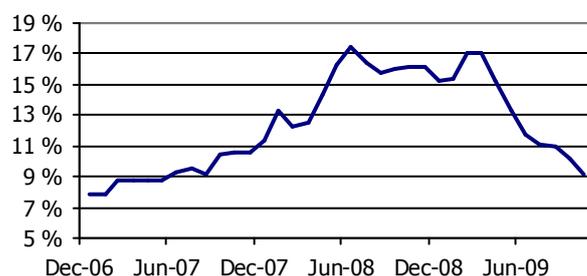


Source: Kaliningradstat (2009)

Consumer inflation at the lowest point since August 2007

Consumer prices declined for the fourth month in a row in October. This decline brought the annual consumer inflation rate down to 9.2% – the lowest since August 2007. Food prices, which were the main driving force for consumer inflation growth in 2007-2008, are now pushing consumer inflation in the opposite direction: they grew only by 4.7% in the first ten months of the year compared with a 9.2% price growth for non-food consumer goods and an 11.7% for service prices.

Consumer Inflation, y-o-y



Source: Kaliningradstat (2009)

Some business highlights

- Czech PPF Group bought a controlling stake in Advantage Group (ADG), which owns, among other properties, an office and retail center in Kaliningrad and also has two hotels under construction there (for 276 and 180 rooms).
- Novaport, owned by Roman Trotsenko, paid RUB 204.9 million (EUR 4.7 million) for a 25% stake in the company, Kaliningrad international airport, which manages Kaliningrad's airport Khrabrovo.
- Avtotor started assembly of Opel's cars – the Astra and Zafira models – on its Kaliningrad's plant in October. It plans to start welding and painting operations in 2010-2011.

Belarus is open for co-operation

By Sergei Sidorski

The Republic of Belarus is a country populated by 9.8 million, occupying a territory of 207.6 thousand, which places it at No. 13 in Europe, and located in central Europe, geographically.

The first decade of the 21st century became a period of transition to a market-oriented economy for the Republic of Belarus. This is now a multisectoral economy, with necessary legislation put in place to help it develop and market infrastructure being currently finalized. There have been improvements made to the structure of production and consumption, large-scale projects launched both in industry, agriculture and in health care, education, housing construction and landscaping.

Over the period, Belarus economy would post an invariably robust rate of development which allowed it, as estimated by the UN (Report of 2009), to qualify into the group of countries with high level of development and run under No. 68 in the Human Development Index, ahead of all CIS countries (Russia – 71, Kazakhstan – 82, Ukraine – 85). The Gross Domestic Product per capita in 2008 was \$ 5.9 thousand.

Pivotal to Belarusian economy are large industrial enterprises accounting for 27-28 per cent of the national GDP. Belarus specializes in the production of machinery, chemical and petrochemical industries, wood processing. The light industry and production of building materials are actively developing. Currently, 90 per cent of the goods exported by Belarus come from the industrial production.

Traditionally, there is a **special focus** in the country on the **agricultural complex**. The agriculture of Belarus encompasses 8.8 million hectares of cultivated lands, of which 5.5 million hectares arable. The country produces largely more major types of agricultural produce per capita (other than grain) than CIS countries and twice as much milk as the US and countries of Western Europe.

The significant potential of the country, exceeding its domestic needs, makes **foreign trade** an overarching priority. Today, we trade with over 170 countries, the world over. Since 2000, our exports of commodities and services have been 4.5 times up to reach \$ 32.9 bn. in 2008.

Key foreign trade partners of the country include Russia and the European Union member states. In 2008, the EU secured No. 1 position in terms of imports from Belarus (43.9 per cent of the total volume). There is successful co-operation with the Baltic countries under way, posting an aggregate turnover close to \$ 11 bn. (excl. trade with the Russian Federation) which is 15 per cent of the total Belarusian foreign trade. Among major trade partners of Belarus in the region are Germany, Poland, Latvia and Lithuania.

The country steps up consistent measures to diversify its export supplies, with new markets and areas explored and tapped in a most active manner. Even though the Russian Federation and the EU remain to be the largest consumers of Belarus commodities, supplies to Asia and South America have recorded a dramatic increase.

In 2009, the country was faced up with the effects of the global financial and economic crunch. Its negative repercussions for Belarusian economy implied, in the first place, shrinking foreign demand leading to the falling volume of exports and production in the exporting enterprises.

However, thanks to the timely crises management measures that were worked out and have been implementing by the Government of Belarus the macroeconomic stability in

the country has been preserved, the landslide of production in the key spheres of economy has been evaded. The crises management program of the Government of Belarus includes several aspects. Among them are economic environment liberalization; support of real sector enterprises, exporters in the first place; budgetary expenditures optimization; promotion of domestic demand; improvement of the financial system stability, narrowing of the external trade deficit.

As a result in January-October 2009 the national GDP amounted to 99 per cent (against the same period of 2008), industrial production output – 95.5 per cent, whereas in all Belarus' neighboring states, except Poland, considerable GDP falldown is in evidence. Thus, in six month of 2009 such downfall made up 10.5 percent in Russia (against the same period of 2008), in Ukraine – 19 per cent, Lithuania – 16 per cent, Latvia – 18 per cent, in the EU as a whole – 4.8 per cent.

The social stability is being preserved in Belarus. In January-September 2009 the population's real income level rose by 2.8 per cent. Full-scale financing of all social programs is carried out; pensions and social allowances are being paid in time. The rate of unemployment in the country does not exceed the pre-crises figures, and at the year-end will not surpass 1-1.5 per cent.

One of the main interests of the state is to create favorable investment climate and ensure protection of investors' interests. To reach this goal a lot has been done on reduction of administrative barriers, liberalization of price formation, customs regulation, reform of property relations. During the last five years the flows of foreign investments to the country have increased 7.5 times, direct ones – 4.4 times. More than 4.2 thousands of organizations with foreign capital from almost 100 countries work in Belarus. Among our main partners are Russia, China, Germany, Austria, the Middle East and Latin America countries.

International organizations (World Bank, Heritage Foundation, IFC and UNCTAD) have registered the improvement of business environment in our country. According to "Doing Business" in 2009 we moved to 58th place (27 positions in one year).

A "B+" sovereign credit rate given to Belarus in 2007 and confirmed this year proves the advantages of cooperation with our country.

Due to our favorable geographical location one of the perspective directions for attraction of foreign investments is the development of transport infrastructure and logistics. A strategic interest for the Baltic region countries represent creation of transit system and logistical services for dynamically developing flow of goods going through the territory of Belarus.

Interaction in the field of energy is also an important direction of development in the region. Belarus actively cooperates there with Lithuania, Latvia and Poland.

Even in the context of global economic crisis Belarus has always been a reliable and stable partner, open for mutually beneficial cooperation.

Sergei Sidorski

Prime Minister

Republic of Belarus

A Latvian view on regional security challenges

By Imants Lieģis

The Baltic Sea regional security challenges need to be viewed in general through the prism of differing security actors. For the purpose of this article I would define them as being three – NATO, the EU and Russia. The latter actor is a member of neither NATO or the EU, but in considering regional security, both these organisations' relations with Latvia's important neighbour have a crucial impact on regional security.

Latvia sees security and defence being provided primarily through NATO. The 1949 Washington Treaty security and defence guarantees from which we have benefited during the last five and a half years of membership are fundamental. Never in the history of the nation has Latvia been so secure since joining NATO. The Atlantic Alliance, which ensures the presence of the USA in Europe, has celebrated 60 years of being the most successful military Alliance ever. The best description of NATO was given by its first Secretary General, Lord Ismay, who stated that NATO was there to keep the Americans in, the Russians out and the Germans down.

Although in many ways this was a Cold War description, I cannot agree with another version of the same quote that was doing the rounds of the conference circuits. Namely today, NATO is kicking the Americans out, bringing the Russians in and the lifting the Germans up. At a time when the primary attention of the new US administration is being directed towards other parts of the globe (China and India) and Europe appears to be slipping off the main agenda, the regional challenge in the Baltic area and beyond still relates to "keeping the Americans in". NATO is the main player which must continue to ensure this US presence.

The European Union remains an important actor in the field of defence and security, but cannot replace NATO as our security provider. The recent ratification of the Lisbon Treaty is welcome in the context of defence and security. But it needs to be acknowledged that the defence commitments in the Treaty are more of a political nature and cannot be viewed as a substitute to the military commitments of NATO.

Even after over 5 years within NATO, we still see the need for reassurances. This is one of the main challenges for us as NATO prepares its new Strategic Concept. For the first time we are able to give a direct input to the process of preparing the new strategy. A former Latvian Ambassador to Washington and NATO, Aivis Ronis, has been appointed as Estonia's Lithuania's and Latvia's joint representative on the panel headed by Madeleine Albright to prepare recommendations for the new Strategic Concept.

Why do we see the need for reassurances? The regional security situation has changed since we joined NATO. Cyber attacks have appeared on the agenda. Our neighbour,

Russia, militarily attacked another of its neighbours, Georgia in August 2008. This changed the security situation in Europe given that this was the first invasion of a sovereign country since the downfall of the Soviet Union. One of the reasons Russia for this action was that it was necessary to defend Russian nationals in Georgia. Since then, Russia has approved in law the right to take such military actions abroad to defend its nationals. In addition, most of the Baltic regional countries were aware of the large scale exercises ("Ladoga" and "Zapad") conducted by Russia and Belarus, together and separately, during August and September 2009. One of the scenarios used was an attack on NATO member states so as to isolate Estonia, Latvia and Lithuania from the Alliance. There was even talk of a nuclear weapon being used against Poland. Regrettably, Russia still seems to regard NATO as an enemy despite the fact that enlargement of the Alliance has provided greater stability to this part of Russia's border.

In awaiting reassurances from NATO's new strategic concept, we in turn will continue to show that we are responsible members. Despite considerable financial restraints on Latvia's defence budget (in 2010 we will have just less than 50% funding than in 2008), I have ensured that our ongoing engagement in the NATO operation in Afghanistan remains our top priority. We will retain our current troop level – 175 soldiers – which has indeed been increased by some 10 soldiers during the course of the year. We are privileged to be part of the Norwegian led PRT in the North of Afghanistan, whilst engaging in the OMLT with our US partners in the more dangerous Eastern border region with Pakistan. Even as the new approach towards this operation (in which all the Baltic regional EU and NATO members are engaged) emerges following President Obama's announcement, we are grateful to our partners for their understanding about the limits of our future participation.

I feel confident that after five years of membership in NATO and the EU for Latvia and our two Baltic neighbours, regional security and stability has improved beyond what we imagined in 1991, when we regained our freedom.

Imants Lieģis

Minister of Defence

Latvia



Us and them

By Päivi Lipponen

Russian democracy is built around a very centralised state combine with a strong sense of national identity

Nikolai Gogol neatly depicts the scene of the 19th century tsarist Russia in his play "The Inspector". Moscow sends an official on inspection duty to a small town. So the local mayor frantically tries to put things in order. Before the arrival of the Inspector hospital patients are sent home, so that the quality of care can not be doubted. Graft is prohibited. The judge reassures the mayor that no one will be able to make any sense of legal decisions handed down by the court. And the mayor suggests that when explaining why the church has not been built to blame it on the fire, even though the money was awarded five years ago for that purpose. Furthermore, the mayor instructs the postmaster to open all outgoing letters so as to stifle any complaints to Moscow. The postmaster gleefully replies that he does just that all the time, being of an naturally curious disposition."

When the satire first appeared it aroused the ire of Russian officialdom. It was not permitted to blaspheme Holy Russia. Gogol had to go into voluntary exile. Back in the 19th century, there was no political opposition to the tsar and his government officials. At that time, writers were very much the conscience of the nation. Only they as members of the intelligentsia, had the courage to speak out and lament the lack of political rights under the regime.

How much has changed in Russia from those days?

Russia has never been a democracy as we understand it in the West. Russian power structures have evolved and been developed down through the centuries. The Chronicle of Nestor records that in 862 Rurik was called on to rule over the slavs. At the same time in Europe the Frankish Empire was being divided up and the Vikings were trading in the Gulf coast.

Not everything has to be accepted, but we Europeans must learn not to focus on deficiencies in Russia. The debate on Russia is dominated by a one sided perspective -how we wish Russia to develop. Nord Stream's pipeline project is a case in point. There are similar tubes passing through the seabed, but this pipeline is said to increase insecurity and environmental risks. Some seemed to have invented a tube, which has only one end.

Europeans should have a keener desire and ability to understand Russia. Only then can we build equal interaction.

The Russian saying that "the sun is in the high sky and the Czar is far away" means that central power has always been strong. By extension local administration has always been underdeveloped. The central power has been autocratic and the relationship to the citizen has been very authoritarian. When political decision-making, tax levies and revenues and the economy are concentrated in Moscow, people's everyday survival has been built around local networks and community-based resources. When there is no civil society,

there can be no political party system. Anna-Leena Lauren asks why the Russians would want to experience solidarity with the community when there is no solidarity with them. Modernization becomes possible when citizens feel that compliance with laws benefits them.

Russia is a very multinational state. It combines the strong national identity, which is based on the belief that Russia is a great power and it has developed its distinctiveness through historical and cultural development. Greater Russia is unique, that is the message taught to schoolchildren.

This deep sense of patriotism is to a large extent born out of a feeling of being threatened. Russia feels that the country has been under attack throughout its history, from the East and West. Russia perceives itself as a peacemaker. Its expansions have been assistance to neighbours and civilization exports. From this point of view: Russia has sacrificed a lot for Europe, when they rescued it from fascism. How has this achievement been rewarded, the Russians ask.

Admittedly, the Soviet Union broke up without a military conflict. Russia has allowed the old enemy to expand into its former sphere of dominance.

The Kremlin views the West's concerns over the degree of democracy in Russia as something a kin to crocodile tears. It feels that export of democracy is just an excuse for Western powers to interfere in other countries' internal affairs and undermine the state. Russia has created its own version of democracy. To the Russians, Europe does not seem to have much to offer to them.

The political elite want to make Russia a superpower again, they want a Russia that is to be ready to do great things again. This status can be achieved only if the state is centralized and strong enough. All that threatens this goal must to be removed. Citizens on the other hand value stability. They want to get their pensions and salaries on time. Above all, they want to be proud of their country and be able to have trust in the future. President Dmitry Medvedev has a vision for the future: Russia must diversify its natural resource based economy, develop its political decision making and reform the judiciary. These changes are necessary for modernization.

Europe should seek partnership with Russia. It may not be wishful thinking that through closer cooperation Europe can influence Russia. Russia must in any case adapt to the international community rules, but Russia can not be changed by Western orders.

Päivi Lipponen

Ph.D., Member of Parliament

Finland



Place and role of the Russian-Finnish economic cooperation in the Baltic Sea Region

By Valery Shlyamin

The Global financial-economic crisis which has only started to diminish particularly vividly depicted the new role of Governments, revealed the importance and significance of strategic approach and elaboration of economic development strategies on the state level. The crisis painfully affected national economies of all the Baltic Sea region states including Russia and Finland and displayed high level of economic integration.

It's known that Finland is one of the major trade partners of the Russian Federation. In 2009 the crisis has quite adversely affected the volume of bilateral trade (diagram 1). Trade turnover dropped to almost 50%. The crisis clearly indicated the bottle neck in the structure of trade – predomination of raw material trend in the Russian export (diagram 2).

We estimate the overall loss of jobs as the result of trade downfall in 2008-2009 at the level of 25 thousand jobs in Russia and 16 thousand jobs in Finland. The estimation is based on the prevalent trade patterns and branch labour productivity data in both countries. Supposedly in current conditions in order to reinforce the competitive advantages of Russia and Finland it's important to search for the new common grounds and strategic guides mainly in the business sphere.

Within all the diversity of our interaction fields the most distinct perspective is seen for the joint initiatives in the spheres of energy and environmental technologies, forestry, transport and logistics fields, high-tech branches, productive cooperation in manufacturing high added value goods including electronics, communication facilities, food production for both - domestic markets and joint entry to third countries markets.

The Baltic Sea region located in the periphery of the European economic centre is highly dependant on external goods and services trade which reinforces the significance of transport infrastructure as the factor of economic growth. Forming the eastern border of the European Union and the Baltic Sea region Finland plays a unique role in creating the trade and economic bridge between Europe and Russia and in perspective in between Europe and Asia. In the recent years transition of goods strongly contributed to the development of the countries' transport and logistics and strengthened the Russian-Finnish trade ties.

Start of the Northern Dimension Partnership on transport and logistics will become an efficient tool of infrastructure projects coordination with a purpose of transport connections development in the Baltic Sea region and increasing the region competitiveness in the world trade markets as well as the region potential as the EU gate to Asia.

The first internal EU strategy on the Baltic Sea region forms an important step representing the new approach to cooperation within EU and shall undoubtedly become a significant factor of the Baltic Sea region activities coordination. Within the Baltic strategy the Northern Dimension policy should become a substantial basis for strengthening the cooperation with Russia but at the same

time we find it vital to refer to the existing experience of joining the strategic interests of member-states in particular Russia and Finland. The Finnish action plan on Russia, cross-border cooperation strategy between Finland and Russia as well as the regional programmes on cross-border cooperation are all of special notice. We strongly believe that economic cooperation in the Baltic Sea region should be carried out in particular on the regional level. In this context it's important to learn to see and consider each others interests. That is why cross-border cooperation is assigned its unique role. Implementation of 5 cross-border cooperation (ENPI CBC) programmes between the border regions of the European Union and Russia with the overall financing of 437 mln. Euro including 103 mln. Euro of Russian co-financing will be a substantial implement of the designated initiatives. In this respect it's extremely important to carefully approach the process of mutually beneficial projects selection and propose the most deserving ones reflecting the interests of SME as a whole and particularly innovation-oriented.

The "Euro Russia" Forum revived as the joint project in 2009 with an active support from our Trade Representation fully meets the expectations and modern challenges and may be considered as an example of the successful project-backing of the Russian and Finnish national strategies. The main idea which forms the basis of the "Euro Russia" Forum is the eagerness of the Russian and Finnish executive authorities to support the building of mutually beneficial trans-border entrepreneurship network with a focus on SME, technological processing production of goods and services. This entirely complies with the Russian strategic goal – creation of competitive production and effective integration into the world economy; as well as Finland's goal to use the natural advantages of neighborhood with Russia. We suppose that involvement of business-partners from other Baltic Sea region countries would be quite natural.

Development of the productive cooperation between Russian and Finnish enterprises as well as interested companies from the Baltic Sea region is what we consider to be the most substantial reserve of the foreign trade growth.

The major goal of the external economic links between Russia, Finland and the Baltic Sea region states is setting up the strategic partnership on the basis of scientific, technological, industrial, transport and energy cooperation with a purpose of creating the common economic space. This forms the basic key for increasing the competitiveness of both Russia and the whole Baltic Sea region.

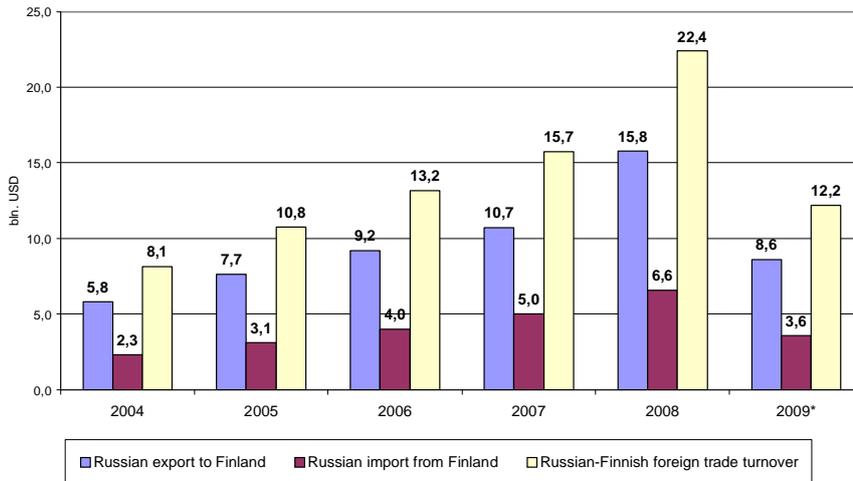
Valery Shlyamin

Doctor of Economics

Trade Representative of the Russian Federation in Finland

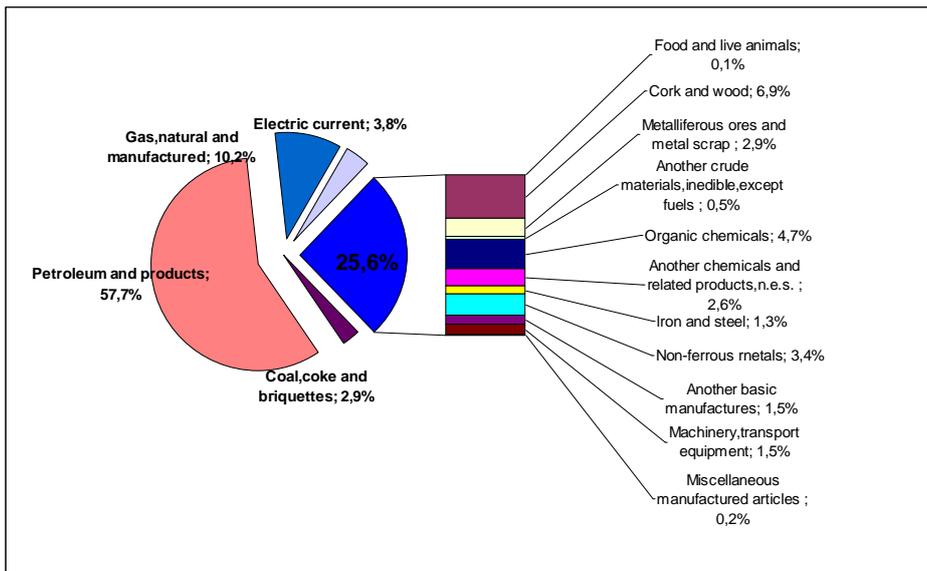
Russia

Russian-Finnish Foreign Trade in 2004-2009



Source: Federal customs service of Russia; * - estimated

Structure of Russian Export to Finland in 2008



Participation of NGOs in the Baltic Sea area cooperation

By Merja Hannus

The Baltic Sea area has favourable possibilities to develop a new kind of unprejudiced multi-faceted interaction and network between citizens and cultures. The high level of economic development of the area, as well as efficient telecommunication and traffic networks further the creation of a good basis for the growing interest of citizens towards cultures of nearby regions. Promotion of a freer mobility of people, so that also Russia would take a close part in this network, would be in the interest of all Baltic Sea area states.

Many non-governmental actors and NGOs have already for a long time been active in the Saint Petersburg area and they would like to cooperate more closely in the Baltic Sea area. They already took part in the establishment of the Baltic Sea network of NGOs in the year 2000 in Copenhagen. From there began the process, which received its form and content in the Baltic Sea NGO Forum established at the Forum of NGOs of the Baltic Sea countries, organized in Turku in 2003. Some 400 NGO actors decided to establish the Baltic Sea NGO Forum. This Forum has convened annually in the chairman country of the Council of Baltic Sea states, the most recent one took place last year in Latvia. Focal points act in each country as contact link between NGOs. The address of this site is www.bsngoforum.org. On these sites there is information about the annual forums and about the documents, pertaining to them.

The agenda of the Forums includes information on the worries of citizens of the area and on the other hand also on the opinions, concerning the development of cooperation. An issue, which has especially been under discussion, concerns the possibilities of NGOs to act, free crossing of borders by citizens, human trafficking and social inequality, as well as elimination of the same. Issues dealing with the condition of the Baltic Sea and protection of the same have been on the agenda of every yearly Forum. Special attention has been paid to environmental education and the means, by which the sense of responsibility of all people for the future of the Baltic Sea can be awakened.

The interest shown by NGOs towards the Baltic Sea area cooperation was in the beginning of the 21st century greater than at the present time. There are probably many reasons, which explain why this is so and the economic factors are not the most insignificant among them. Public support rendered to NGOs is not very well developed in the Baltic states, Poland and Russia. Between the Nordic countries and even with the Baltic states there are many contacts on the level of citizens, but the more extensive contacts with Russia have mostly to rely on Finland. The other Nordic countries do certainly carry on some cooperation with Russia, especially in the Saint Petersburg area, but not to the same extent as the Finnish organizations. The very poor relations as to cooperation between the Baltic states and Russia influence also the cooperation and activities of the NGOs.

The strong side of the Finnish actors in this field is the implementation of many concrete projects. Many NGOs in

the Karelian Republic, Saint Petersburg and the Leningrad area have as to cooperation good relations with Finnish organizations. The appropriation granted by the Finnish Ministry of Foreign Affairs to NGOs for cooperation with nearby regions of Russia has helped to develop joint projects and undertakings. This sum is not so big, but it has made it possible to carry on cooperation on the grass root level, as well as implementation of many development projects between the regions of Finland and Russia bordering with the Baltic Sea area. The Kaliningrad and Pskov areas have aroused less interest in Finland.

The Nordic Council of Ministers has also to some extent supported the development of the networks of NGOs and their project activities. The Baltic Sea NGO Forums have mainly relied on financing by the Council of Ministers and also on that of the Foreign Ministries of the host countries. Each year this financing has however been the result of lengthy discussions and complex project applications. The uncertainty as to financing has without doubt tired many organizations, and this has probably been one of the reasons for the slight decrease in the readiness to carry on cooperation. Finland would now have good possibilities to further the development of the Baltic Sea area cooperation at citizens' level by allocating to this cooperation more permanent resources.

Finland will in 2011 be chairman of the Nordic Council of Ministers and could then especially set as its goal to create closer contacts between the civil societies of the Nordic countries and Russia by way of encouraging and supporting networking between NGOs. The Finland-Russia-Society has a vast experience in the development of cooperation with Russian NGOs and this experience could now be made use of. Interest towards this issue is for sure to be found among the NGOs and actors of Northwest Russia. It would be great, if this kind of a meeting could be held in the only real metropolis of the Baltic Sea area i.e. Saint Petersburg.

The Baltic Sea, its future and strengthening of contacts between cultures and citizens would be natural issues for discussion at an NGO meeting. The special issues, concerning cooperation in the North, could also be brought up. The most important issue for consideration is however, how to promote the operating possibilities of NGOs and in what way these organizations could contribute in the best possible way to the materialization of well-being and a closer interaction between people in the area.

Merja Hannus

Secretary-general

Finland-Russia-Society

Finland



Riga nowadays

By Nils Ušakovs

Riga has always been the city with strong development potential and today it still remains the engine for the national economic growth, being also one of the most significant players in the Baltic Sea Region that has been recognised as one of the most attractive areas of the world for business. Nowadays development of the transport sector and large public infrastructure projects, as well as attraction of investment and strengthening the relationship between the West-East and the North - South have been set forward as the key priorities of the Riga City.

Riga is the centre of a well-developed transportation and communications infrastructure that includes railways, roads, pipelines, port facility and the airport, all of them having a great capacity for further growth and development.

Today the city fulfils the function of the transportation hub supporting the link between the Eastern and European markets.

The Baltic Sea has always been the source of prosperity and well-being. Since its foundation Riga has grown and developed together with its port. The advantages of Riga over the neighbouring ports in terms of distance provide the most favourable conditions for the development of economic relations.

Thanks to the developed motor-road and railway network, the Riga Port is directly linked to the main consumption centres and extraction-processing regions of Russia and the Commonwealth of Independent States (CIS). Presently up to 80% of the cargoes handled at the Riga Port are transit cargoes to Russia and the CIS states.

In 2008 the cargo turnover at the Riga Port has reached more than 29 thousand tons and the further increase of cargo turnover at the Riga Port plays enormous importance for the city economic development. Fulfilment of the Riga Northern Transport Corridor project will additionally provide possibility to connect the Riga Port to the road network of European significance and increase the competitiveness of the East-West transport corridor in Latvia.

Riga has the largest international aviation company in the Baltics and the main air traffic centre in the region - the Riga International Airport that renders both- aviation and non-aviation services, attending national, as well as international

airlines. It is one of the few European airports that services full - service and low costs airlines simultaneously. In 2008 RIGA International Airport attended 3.6 million passengers, which is 16.8 percent more than in 2007. In the first six months of 2009 the number of passengers welcomed at Riga International Airport has grown by approximately 10 per cent year on year. This year the Riga International Airport has been awarded the prestigious RoutesandOAG Airport Marketing Award in Europe as the best airport in Scandinavia. This prestigious award serves as a proof for the successful development of the relationship with airline partners.

Accessibility of the city has enhanced its attractiveness for being a place to meet and share viewpoints, to feel the atmosphere of personal freedom and global thinking.

In recent years the city has been the host in a wide range of different significant international events.

In 2006 Riga welcomed two events of a global significance - the NATO summit and the World Ice Hockey Championship 2006, having proved itself as a reliable organiser and excellent provider of facilities.

The city has also a rich cultural life and it is abundant with social events. In 2014 Riga will be nominated the European capital of culture.

In 2010 it is scheduled to host the Mayors` meeting of the European Union, CIS and other partner cities. This event will contribute to raising awareness that cities have the key role in economic development in local, regional, as well as global context, as they are the centres that attract investment and develop partnership among public, private and academic sectors.

Nils Ušakovs

Chairman

Riga City Council

Latvia



Not the western or eastern, but the Baltic Sea

By Edgar Savisaar

Media creates, maintains, represents and strengthens the identity of today's countries in the world. For example, we could take the American CNN, the British BBC World, the Chinese CCTV9, the Russian Russia Today, the French France24, or even the Arabic al-Jazeera. The integration of the Baltic Sea countries will remain a dream written down on a piece of paper, until we promote the region's identity continuously, every day, every hour and every minute, through its very own media channel.

The European Union Baltic Sea Strategy, approved by the European Council, gives a considerable amount of attention to the subject of energy security and the energy isolation of Estonia and some other countries. The importance of creating physical access to the electricity market is emphasised and the environmental protection aspects of the energy sector are also mentioned – in relation to transporting liquefied gas by sea... However, the strategy doesn't even mention the largest Baltic Sea project in process – a gas pipe linking Russia and Germany. Although the strategy does list dozens of other infrastructures, which will be built in the Baltic Sea region, the effect (financially, economically and especially politically) of even the largest of them, the 19-kilometre Fehmarn Belt bridge, connecting Denmark and Germany, is not even comparable to the 1,200 kilometre Nord Stream project.

Today, we find ourselves in a situation where a project that brings together the eastern corner and western edge of the Baltic Sea will at the same time separate its northern and southern shores. This doesn't have to be so, and the establishment of a shared information space would serve as a tool in aiding to resolve this and the many other problems that keep the people of the Baltic Sea region separate.

It's quite obvious that without a common information space we cannot count on the implementation of the other policies that are planned in the strategy, as all of these assume the commitment of politicians to the established goals – both today and in the future. Politicians, however, will need the support of their people for that in democratic societies. The media channels that currently operate are unable, strictly within a national perspective, to create and explain our common agenda to the Baltic Sea nations.

The public of Estonia, Latvia, Lithuania and Poland was and largely still is against the gas pipeline, while the Nordic countries have favoured it. This is attributable to the fact that the media of the opponents emphasised the risks while the enthusiasts focused on the opportunities. The Nord Stream case is a good example of the fact that we do need a common information channel, especially concerning projects that extend to the Baltic Sea region as a whole. The presence of a common information channel would definitely have given a rational overview to the Baltic Sea countries of the rather controversial subject of the gas pipeline. And, of course, politicians would then have been able to discuss the largest Baltic Sea project within the context of the most important political framework documents of the region.

Compared to the so-called hard investment projects (roads, harbours, bridges – the amount earmarked for such undertakings exceeds 20 billion EUR), which are dominant in the strategy among the projects that are being launched to increase the economic growth and attractiveness of the Baltic Sea region, the expenses related to the creation of a common media channel would be negligible, while the influence of such a channel to the real integration and competitiveness of the whole region would be incomparably

bigger than any bridge, tunnel, or railway could ever be. If we were to add cross-border public and private sector e-services to the central media output, the channel's interconnecting effect on the region could only be comparable to the adoption of the common currency.

Considering the audience number, the Nordic countries clearly have one of the strongest public broadcasting systems in the world and TV channels that receive considerable funding from the state also exist in all the three Baltic states. In the Nordic countries, private multinational media groups control the media market of the whole region. And still one could count on one hand the number of media outlets with newsrooms that regularly share content between countries, them being the BNS news agency (Baltic News Service belongs to Finnish Kauppalehti group of Alma Media) and the Estonian online media portal Delfi, both of which operate in the three Baltic states, and the Baltic Times weekly newspaper; and that's the lot, at least on the eastern shore of the sea. The Nordic countries don't even have that much to their name. Currently, there is no media channel that has a significant number of readers/listeners/audience and which focuses in the Baltic Sea region as a whole.

For such a channel, the working language would be an important issue to be considered. And for more and more people around the sea, the only reasonable answer would be – the English language. Since EU enlargement, the largest multinational companies have given up the nordiska, which was only convenient for one party, and have switched over to the English language for running the media groups that cover the whole region – both for practical and strategic purposes. It's time to take the language exchange that has already taken place on the level of the elite to mass media.

However, all the countries that would participate in the project (as much as eleven) would certainly be able to have a voice-over option in their national language, as is the case with the Euronews. For the external promotion of the region there could, aside from French and Spanish, be provision also for other global language options such as Japanese, Chinese and Arabic (subtitles).

Preceding the exchange and sharing of media content and a number of joint media ventures between the countries, in both public and private media, would considerably contribute to the establishment of an international public broadcasting team. Most certainly, the exchange of such programmes should be subsidised by the governments and the European Union. Apart from focusing the audience, this would also bring media teams closer to each other, which is inevitable in launching a channel that covers the whole region.

Estonia is the only country in the world that calls the sea the "Western Sea" (Läänemeri) in official documents. Our Finno-Ugrian friends, the Finns, translate it as the "Eastern Sea", (Itämeri), translated from Ostsee, as the sea is called in the Swedish, Danish and German languages. For Hungarians, it's the Baltic Sea, and this is also how the Latvians, Lithuanians and the Polish, living south of us, call it. For centuries, it has been known to the rest of the world as the Baltic Sea, including the two major working languages of the EU, English and French.

For further real progress with the Baltic Sea region, we need to agree upon a common name for the region. There could be no serious discussion of external marketing if the region is without a single name. To say nothing of the odd situation in which one country would be using the "Western Channel" logo in the upper corner of the screen, another the

“Eastern Channel” and the majority – “the Baltic Channel”. Estonia could make a short, yet important step for the identity of the Baltic Sea and start using the name “Baltic Sea” again – as the sea was officially known during the first decade of the existence of the country after 1918. As the Baltic Sea region develops, the Nordic countries, which use the English language for the purposes of international communication, will sooner or later accept the fact that a name that is familiar to the whole world would be used to describe the sea that we all are sharing (maybe getting some inspiration from Estonia, too!).

Finally, I have the pleasure of recognising that the issue of the common identity of the region hasn't been fully ignored in the Baltic Sea Strategy documents. Although it has been stated in the security package that the uniformity and identity of the region comes from the Baltic Sea itself, the chapter on economics, and in particular the section on tourism

development, also refers to the need to create such an identity. The development of regional Baltic Sea identity has been named as the last – hopefully not the least – activity in the list of horizontal actions of the action plan for the implementation of the strategy – and a shared history book and joint hosting of some bigger sports event would contribute considerably to accomplishing this objective.

Yes, this is too little and too late – but better this than nothing. This reference will help to make the Baltic Sea region a green, wealthy and safe place.

Edgar Savisaar

Mayor of Tallinn

Estonia



From Saimaa to continental Europe

By Seppo Miettinen

The City of Lappeenranta in South Karelia, Southeast Finland, is located on the southern shore of Lake Saimaa, the fifth largest lake in Europe. Connection to the Baltic Sea was established in 1856 with the completion of the Saimaa Canal.

Due to its location near the Finno-Russian border, Lappeenranta quite literally serves as a gateway between the EU and Russia. In addition to three border-crossing points (Nuijamaa, Vainikkala, and the Saimaa Canal), the city has an international airport.

The border region has endured several years of war and oppression over the decades. Today, Lappeenranta's location greatly benefits not only the business sector but also education and culture. The fall of the Soviet Union and the subsequent development of Russia have provided the area with completely new opportunities. For instance, nearly 700,000 Russian tourists visited Lappeenranta last year and the total of tax free purchases made in the city is only second to Helsinki.

During Viking times, trade routes extended from Karelia to Novgorod and all the way to Constantinople via the Russian river system. Nowadays Lappeenranta is a hub for road, railway, and water transport between Finland and Russia. Excellent and regular connections ensure quick access to the rest of Finland and the world. Making a day trip to Brussels is just as convenient and easy as travelling more locally.

Good connections have throughout the ages been considered vital to the success of our region. In the Middle Ages, Lappeenranta gained prominence as a centre of the fur trade, and also offered thriving markets for fur and food merchants. Although located far from Vyborg and St. Petersburg, Lappeenranta was never left behind in development in the times before the Second World War.

Maintaining excellent connections to the coastal towns and cities in the Baltic Sea region is vital for Lappeenranta's future. Via Vyborg and St. Petersburg, Lappeenranta has a direct access to Germany and the Netherlands and other centres of commerce in the coastal Europe. In the past, these same channels served to spread cultural influences and knowledge of the newest inventions and world's events to Lappeenranta.

Although the distance between Lappeenranta and Vyborg is only 50 kilometres, land and river connections were considered inadequate. The possibilities for constructing a canal between Lake Saimaa and the Baltic Sea were mulled over as early as the 16th and 17th centuries, mainly to ease transportation of wood and timber. The new waterway, the Saimaa Canal, finally became a reality in 1856.

The Saimaa Canal has from the outset been vital to the travel industry as well as to transportation and trade. With its automated lock gates, the Canal is quite an exotic route in the middle of the unspoiled lake environment, which explains the popularity of visa-free cruises between Lappeenranta and Vyborg.

The Second World War brought radical changes to Lappeenranta. Before the war, Vyborg was the second largest city in Finland. As a highly significant centre of international trade, the city was a multicultural and multilingual community.

The City of Lappeenranta continues to cherish the heritage of Vyborg. In the modern, constantly changing world that values networking above all else, Karelians' famed social skills and innovativeness are precious assets.

In the years preceding the war, Vyborg had no university. In Lappeenranta, the Institute of Technology (now the Lappeenranta University of Technology) was founded in 1969. The strengths of our university include a focus on internationality in general and knowledge of Russian trade and culture in particular, innovation cooperation, and active participation in national university networks.

Today, Lappeenranta is an international university city and the most significant centre of Russian operations that works actively towards creating connections between the European Union and Russia. We have great hopes for the Finnish-Russian Innovation University, which is being developed by the Lappeenranta University of Technology together with other Finnish and Russian universities. The objective is to establish a top-level educational and research cooperation network in the fields of economics, technology, and design.

Lappeenranta is equally close to Helsinki and to St. Petersburg. This means that a total of eight million people live within a two hundred-kilometre radius of our city. If we can find new ways to encourage travel to Lappeenranta, tourism could become an extremely successful trade in the region.

Every year, more foreign tourists visit Lappeenranta than any other city in Finland except Helsinki. Opened in autumn 2009, the new flight connection from Lappeenranta to Europe via Riga attracts not only business travellers but also researchers and adventurous tourists to our city.

The Saimaa region is an exotic destination for people living in continental Europe. The lake is not enough on its own, however, which is why we are constantly adding to the range of services on offer.

Our objective is to enhance the attractiveness of the Saimaa region by introducing new amenities such as spa resorts. We are also developing Energiamaa, a new energy production-themed adventure and science centre. The centre is being developed in cooperation with the Lappeenranta University of Technology and will be an ideal destination for the families and people of all ages.

Connections with Vyborg and St. Petersburg, which were severed during the Second World War, have been revived in recent decades. Together with its old partners, Lappeenranta is still part of the network of towns and cities in the Baltic region. This is reflected in the expertise of our university. The Northern Dimension Research Centre, NORDI, for example, which is part of the Lappeenranta University of Technology, specializes in technological and economic questions relating to Russia and the Baltic region. Typical of its home region, the institute's special fields of expertise include economics, business operations, innovations, energy, and logistics.

Seppo Miettinen

Mayor of Lappeenranta

Finland



Gotland – pearl of the Baltic!

By Eva Nypelius

Gotland is the Baltic region's most creative and magical place, characterised by nearness, sustainable growth and love of life.

This is the vision for Gotland, located in the middle of the Baltic Sea and Sweden's largest island, with over 57,000 inhabitants. We are just as close to the Baltic coast as we are to the Swedish mainland. 80 million people live within a radius of an hour's flight. Gotland's vision guides and drives our work to achieve the region's objectives for 2025:

- To grow to 65,000 inhabitants on Gotland
- Local prosperity will be among the best in the country
- Gotland will be the natural meeting place in the Baltic region
- The local population will be in good health and be the most contented in the country
- Gotland will be a world-leading island region on environmental and climate issues

These are lofty ambitions, but I have every confidence that we can achieve them by working strategically. Gotland is a dynamic place to live and work – all year round! All sorts of positive things are happening on Gotland right now: the population is growing, we are riding out the recession well with low unemployment, the island's business community is confident about the future, house building remains strong and many people are showing an interest in Gotland and the opportunities it offers.

As I mentioned, Gotland has come through the recession extremely well. This is due in large part to the fact that we have many small businesses with just a few employees. Small businesses are often more flexible and able, for a period, to adapt production to survive temporary dips. Gotland has a greater density of companies than any other county in Sweden, and also boasts the largest proportion of female entrepreneurs. Agriculture and tourism are the two largest industries on the island. Manufacturing is a small but important labour market that includes production of timber products, cement, lime and boats. Gotland is also known for its talented designers, who are making a name for themselves far beyond Sweden's borders.

There is great potential to increase the value of our products by turning more of our exquisite raw materials such as lime, wood, wool and leather into more refined goods, as has been done so successfully in the food sector. We have plenty of skilled and innovative entrepreneurs focusing on locally produced and designed products. After all, food is a source of pleasure and experience and mealtimes are an important way of bringing people together. We have great potential to develop Gotland as a meeting place, in combination with the island's cuisine, high-quality resources and environmental work. Gotland is an island full of delicacies and culinary experiences.

Gotland is a modern meeting place in the middle of the Baltic Sea. We are active participants in many Baltic networks, including the Baltic Islands Network (B7). We also host the secretariat for the Baltic Sea Commission and we are the deputy chair of the modern Hansa network, to name but a few of our activities. Here on Gotland, we have long embraced international relations. We were among the first to start cooperating with our neighbours in the eastern Baltic and before EU membership came about, we issued a white

paper on Gotland and our position in the middle of the Baltic Sea. Since the 1990s, we have had three cultural centres: the Baltic Centre for Writers and Translators, the Baltic Art Centre and Visby International Centre for Composers. We see it as a natural and very welcome development that a whole host of institutions with an international focus have chosen to establish themselves on Gotland, which also strengthens our position as the key meeting place in the Baltic Sea region.

With our strategic location, we also have extensive experience of trade links and international contacts dating back to the Hanseatic League. We are now building further on this, in part through Wisby Strand, the new congress hall which, with its unique location and magnificent views of Almedalen and the sea, will be a new and exciting reason to travel to Gotland. Tourism has seen positive growth, with modern facilities helping to generate more visitors and more guest nights.

Globalisation does not stop at any regional borders. On the contrary, a future-focused region has to realise that we are dependent on the wider world and global developments. The climate issue affects and concerns us all, and may indeed be particularly significant for those of us who live surrounded by water. I believe that the greatest challenge we face in the future is a clean and living Baltic Sea. It is therefore good to see the new Baltic Sea strategy taking up many of these key issues. Back in 1990, the municipality of Gotland became an eco-municipality and now everyone on Gotland is working actively on a broad front to achieve an ecologically sustainable society with sustainable growth on Gotland by 2025. One of our objectives on Gotland is to be the leading island region on environmental and energy issues by 2025.

Environmental and energy issues present major potential for economic development. We have already installed a number of wind turbines and wind power has a key role to play in a sustainable energy system on Gotland. The conditions are in place for investment amounting to SEK 1.5 billion through expansion of wind power on Gotland to 1,000 MW installed capacity with annual production in the order of 2.5 TWh. Expanding wind power will have a positive impact on Gotland society in the form of more jobs and an increased influx of capital. Biogas is another exciting area where, in making use of waste products and so on from agriculture, we're working on a conversion strategy so that we can increase the proportion of biogas used as vehicle fuel.

Gotland is a peaceful and safe place to live, with unique access to nature and culture. Living on the island is a special experience, with the ever-present sea and far-reaching views towards the vast horizon. The climate on Gotland is mild and the air is crystal clear.

Gotland is a region of exciting developments with much to discover, so do accept our open invitation!

Eva Nypelius

Mayor of Gotland

Sweden



St. Petersburg – the centre of innovative development of Russian Federation

By Mikhail Oseevskiy

Saint Petersburg, the second largest city of Russia, often called its "Northern capital city". Located at the crossroads of sea and river routes as well as land thoroughfares Saint Petersburg is the European gate of Russia, its strategic center, the closest to the countries of the European Union.

Saint Petersburg is a young city. It was founded by Emperor Peter the Great in 1703. Today, however, Saint Petersburg is the fourth largest city of Europe after London, Moscow and Paris. Its resident population is over 4.5 mln. people.

For over 200 years our city was the capital of the Russian Empire and we still admire the beauty of its palaces, embankments and parks - Hermitage, Russian Museum, Summer Garden, Petrodvorets - are world known.

Saint Petersburg today is the largest industrial, scientific, educational center of Russia. Starting from 2003 the gross regional product was annually growing by more than 8% and was 91 bln. dollars in 2008. Our strategy is a favourable business climate, economy open to competition, support of innovative projects.

St. Petersburg is the centre of the academic, branch and high school science (more than 11 % of scientifically-educational potential of Russia) which is capable to generate scientific and technical achievements in the diversified areas: hydrogen power, microsystems, nano - and the biotechnologies, new materials and other directions.

The sphere of a science and innovative activity of St. Petersburg is presented by 429 scientific organizations, 327 branch scientific organizations, 78 high school organizations.

In a city work as 85,7 thousand scientific employees, from them about 3 thousand doctors of sciences and over 9 thousand candidates of sciences. At universities and institutes of St. Petersburg 8 % of all Russian students are trained. 70 % of workings out of research-and-production sphere of St. Petersburg were realized in other regions of Russia and foreign countries.

The number of the large and average enterprises of the industry of St. Petersburg which create the advanced industrial technologies, in 2007 has constituted 36 companies. The quantity of the created advanced industrial technologies at these enterprises in St. Petersburg in 2007 has constituted 73 % from total number of the created technologies in Northwest region. The enterprises, using in the activity the advanced industrial technologies more than 230, and applying technologies – it is even more. So, the quantity of the used advanced industrial technologies in 2007 constituted 2985 units – a quarter of all used advanced industrial technologies in Northwest region of Russia.

Comparison of this data shows that the enterprises consuming innovations, much more, than making them. On the one hand, it testifies that in a city the considerable quantity of the enterprises uses innovative technologies; on the other hand – that while is much less than again developed innovative products. It means that already in a near-term outlook the increase in demand at innovations will lead to acceleration of work of the enterprises creating them.

We clearly understand what we want our city to be like in the midterm. The primary goals have been stated in "Programme of Social and Economic Development of Saint Petersburg until 2025". The major objectives are:

1. *Saint Petersburg is a center of science, education and innovation.*

There are 45 universities in Saint Petersburg with over 400 thousand students. We are planning to launch a large-scale programme of innovation promotion on this basis. The

primary areas are precision mechanics, optics, electronics, IT-technologies, pharmaceuticals and biotechnologies.

2. *Saint Petersburg is a trade and transport hub.*

Development of Saint Petersburg as the largest Russian trade and transport center of international significance located at the Baltic Sea provides for measures to stimulate export-import goods traffic via Saint Petersburg or adjacent territories, to simplify the procedure for crossing of the border and customs procedures, to build new customs terminals.

An essential element of development in this direction will be reconstruction and extension of the capacities of the Greater Port Saint Petersburg and construction of new terminals. Construction of the ring motorway round Saint Petersburg is nearing completion. New high speed railway and superhighways for communication with Moscow and a new airport will be built.

3. *Saint Petersburg is a city open to the world, a largest international center of business, political and cultural cooperation.*

Saint Petersburg has become a place of high-level negotiations, including summit talks, conferences, forums, a place where major political and economic decisions are taken. Besides, Saint Petersburg has started assuming a number of nationwide federal functions. In particular, the Constitutional Court of the Russian Federation is already located in Saint Petersburg.

Saint Petersburg is strengthening its role as the cultural capital of Russia, as a venue of festivals, exhibitions and concerts, many of them being internationally significant. We set the task to increase the tourist attractiveness of Saint Petersburg, which will enable us to become a leading European center of international tourism.

Nevertheless, like most cities and regions in the world, in autumn 2008 Saint Petersburg faced with the world financial crisis. We had to prove that city was ready for any difficulties, that the pre-crisis measures turned out to be necessary and timely while the strategic goals for the foreseeable future did not change.

In April 2009 the Government of Saint Petersburg developed and approved the anti-recessionary plan consisting of the following main sections:

- The first section. *Strengthening social protection.*

Over the year since the beginning of the crisis the registered unemployment rate has been still very low: 28 thousand people, although the number has doubled. This is a little more than 1% of the workforce. Such a low unemployment level is ensured both by the dynamic development of the city economy in the recent years and reduction of the population, typical of many European cities.

All the unemployed get unemployment allowances and have a possibility of getting a new profession at the expense of the state. We pay special attention to employment of women, young people and the disabled.

Despite the city budget cut, it fell by 20% compared to 2008, we have decided to raise the salary in the public sector in 2009 – over 280 thousand people. We have raised the allowances and payments at birth of a child to families with children, to disabled people. The total amount of social payments in 2009 will exceed 450 million dollars.

The second direction of the anti-recessionary program is *support of business activity and creation of new jobs.*

It should be noted that this complex of anti-recessionary measures is the most financially intensive one and is implemented, first and foremost, by the federal government. This includes increase of banks' capital, granting credits to

largest industrial consumers and enterprises, stimulation of demand, including demand for motor cars. Saint Petersburg has supplemented the federal program by providing subsidies to compensate some part of the expenditures related to acquisition of modern technological equipment by leasing, improving the employees' qualification, certifying the products.

We pay special attention to support of small and medium enterprises as this is an essential part of the city economy. Saint Petersburg has a leading position in Russia by the number of small enterprises per 1 thousand of residents. We have increased threefold the city budget expenditures for providing grants to first-time entrepreneurs for establishment of their own business, training programs and consultations, participation in exhibitions.

From January 1, 2010 the taxes for small business will be reduced by 30%.

Introduction of the system of contracting via Internet has considerably simplified the possibility for small enterprises to receive a city order.

All these measures have enabled us to create over 15 thousand new enterprises since the beginning of the year.

The third section of the anti-recessionary program is *development of the engineering and transport infrastructure of the city using mechanisms of private-public partnership.*

We have always liked this way of implementing large projects; however, the limited direct budget investments available this year made us boost our efforts and attract private investments in new industries. It should be noted that our strategic consultants in the private-public partnership area are the World Bank and the European Bank of Reconstruction and Development.

This year we have completed the tender for choosing a concessioner for construction of a new city airport: it is an international group headed by Frankfurt airport. Tenders are under way to choose partners for construction of the Western diameter – the first toll superhighway in the city and a tunnel under the Neva River.

In the near future we will announce a tender for construction of a large garbage recycling plant and a highspeed tram line.

The anti-recessionary program - live and dynamical, it is constantly optimized and improved. Analyzing the current situation we can say that the peak point of the crisis passed and we are going up. Unemployment is going down, the bank credit volume is increasing and, apparently, in the 4th quarter we fix the growth of the gross regional product.

I want all interested in development of the business in Russia foreign investors to pay attention to St. Petersburg – its possibilities, prospects and potential are opened for you. I do not doubt that cooperation with our city will be mutually advantageous and interesting to all participating parties!

Mikhail Oseevskiy

Vice Governor

St. Petersburg

Russia



Challenges for Estonian higher education 1991–2020

By Peeter Kross

Similarly to the Estonian society and economy, our higher education system has undergone a rapid transformation after regaining independence in 1991. Estonia, being a small country, has very clearly understood that the quality and successful functioning of the higher education system determines economic competitiveness the sustainability of our nation in the future. Here is a brief overview about the development of Estonian higher education system and remarkable challenges from the last 18 years and for the upcoming decade.

90's – market economy growth period

After the restoration of independence, the utmost challenge Estonia faced was to rapidly reorganize the soviet-socialist education system. A society which was experiencing a series of renewing reforms, had established a real demand to acquire the knowledge and skills needed for in a market economy. It was a time when the popularity of higher education rose at an exceptional rate. During those years the total number of Estonian students doubled, increasing from 25 000 students in 1990 to 50 000 in 1999 and the enrollment rate at universities increased up to 2,5 times. If in the beginning of 90's the number was 6000 then in 1999 it was already over 15 000.

As a result, the number of higher education institutions increased accordingly. At the beginning of 90's there were 20 higher education institutions, including 6 universities and 14 applied sciences institutions. By the year 2001 Estonia had 49 higher education institutions, out of which 16 were universities and 33 applied sciences institutions.

The liberal economic policy, which brought rapid success to the Estonian economy, influenced the management of the higher education system as well. In the 90's the number of self-financed places soared and several new private schools were opened, so that in the end of the decade it had risen up to 21 000 places forming 40% of the total study places in higher education. However, it was not these new private schools, but our public universities which became the biggest paid education providers in Estonia.

2001–2010: period for ongoing growth and maintaining levels of quality.

In the year 2001 the total number of students in Estonia had grown to 60 000, which has remained the peak year for private higher education institutions. At this moment, Estonia had 10 private universities and 17 private institutions of applied sciences.

During this period the main questions and challenges are related to the quality of higher education, and in order to ensure this, international accreditation process for curricula have been implemented, and several changes in law have been made to make the rules and regulations stricter. Beside those steps taken by the government, public universities sign the Quality Agreement, which aim is to regulate Estonian universities "rules of the game". Remarkably firm changes are made, for example, to the universities' research criteria, Doctoral studies and the Owners Equity requirements for the private schools. For the weaker institutions the year 2002 proved to be the beginning of a period of closures and mergers, so in 2009 there are 34 higher education

institutions left, including 10 universities (6 public and 4 private universities) and 24 institutions of applied sciences, out of which 11 are private schools. However, at the same time there was still a rapid growth in the total number of students in the higher education field, rising up to 68 000 for the year 2009. The greatest number of admissions was in 2004, when 19 500 students started their studies. Also self-financed studies went through a remarkable increase. In the year 2009 37 000 students (55%) studied in self-financed places, out of which 12 000 (18%) were in private institutions. State financed positions were occupied by 31 000 students (45%) of the total students number.

Up to now, Estonian higher education system has been focused on academic education (Bachelor, Master and Doctoral studies) rather than applied sciences, which is supported by the fact that in the year 2009 72% of students were in academic programs and only 28% in applied science programs. It is interesting to see, that during the last years the total number of students in the applied science studies has declined, which is a relatively different situation compared to several other countries.

However, one of the most outstanding and positive outcome for that period is that the Estonian higher education system transferred to the Bologna 3+2 system without remarkable problems.

2011–2020: period of declining number of students and insuring the quality in the future

One of the major challenges Estonian higher education has to overcome is the rapidly appearing demographic gap. The years following the regaining of independence brought along rapid changes in the society and unfortunately also decrease in the birth rate as well as a noticeable extensive emigration wave. Between the years 1990 – 2009 total population of Estonia has dropped by 15% which is 230 000 persons. However, the generation from the beginning of 90's forms the major part of the students studying at the universities for the next decade. It's a matter of fact, that during the upcoming 10 years time the number of high school graduates will fall for 40% compared to the period 2000 – 2010. For our higher education institutions this will result in a sharp downturn in total student numbers accompanied by the fact that after joining EU in 2004 the number of Estonian students going for studies abroad has multiplied. Therefore, the future for Estonian higher education seems rather dramatic. Yet, the downward trend in students and educational institutions provides an excellent opportunity to contribute to and increased level of quality in education. In 10 years time, it is certain that Estonian higher education will have made a big step forward, being considerably more international and open to the world than it is today.

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The Eastern Partnership and Ukraine – plus or minus?

By Olga Shumylo and Jakub Parusinski

The Eastern Partnership (EaP) was officially launched in March 2009, as an instrument for regional cooperation on a broad set of issues, including democratization, good governance, energy security, bolstering trade and state capacity building, between the EU and countries in East Europe and the South Caucasus. The EaP complements and builds upon the Eastern Dimension of the European Neighborhood Policy (ENP), introduced in 2004. As the EU's new policy towards its eastern neighbors, the EaP provides a valuable opportunity for regulatory approximation and economic integration. However, the EaP suffers from internal weaknesses, notably a lack of balance between its multilateral and bilateral components. Moreover, its success depends on both sides demonstrating the will power to push through measures and reforms.

The EaP is based on two pillars, a bilateral and a multilateral one (see table). The former component is significantly more valuable to Ukraine, and other EaP countries, as it presents greater opportunities to leverage reforms through regulatory convergence with the EU. This can be developed through Association Agreements between the EU and its Eastern partners that will focus on deepening trade and economic relations. The EU plans to exploit a new capacity-building instrument through Comprehensive Institution Building (CIB).

The multilateral component focuses on four thematic platforms: democracy, good governance and stability; economic integration and convergence with EU policies, energy security; people-to-people contacts. At the moment, there are two flagship initiatives within the multilateral pillar: Integrated Border Management and the Southern Energy Corridor. The EaP also provides a framework for regional development, with an emphasis on reducing social and economic distinctions between regions.

The EU's trade with Ukraine has been rapidly growing in recent years, with average import and export growths of 18.24% and 23.48% over the past five years respectively, making it Ukraine's biggest import and export partner. Also the Union possesses the strongest transformative power for the country. The most important issues in EU-Ukraine relations, and of the EaP's bilateral component, is the creation of a Deep and Comprehensive Free Trade Area¹ (DCFTA). Such a DCFTA would require analogical regulatory approximation, in order to remove 'behind the border' obstacles. This would not only improve trade 'fluidity' between the two partners, but first and foremost it could also improve regulation and transparency in Ukraine. In the future this may further enhanced by the development of a visa-free regime, one of the EaP's objectives.

The Polish-Swedish initiative is welcomed by Ukraine. While it is viewed as a possibility to deepen collaboration beyond the limited framework of the ENP, it is nevertheless seen as an imperfect solution. The first concern about the EaP regards its value-added in comparison to previous initiatives. Indeed, the EaP does not bring in many new cooperation dimensions as many of these issues were already covered by the Black Sea Synergy, the ENP or bilateral agreements. The second concern deals with the organization of the EaP, notably the 'basket' of nations that it deals with, as there is a wide disparity between the levels of institutional and economic development between the East European countries and the South Caucasus.

The EaP also suffers from a certain dissonance between its political ambitions and its financial resources. The latter were initially planned to be limited to the ENP budget, but were ultimately increased in the framework of the European Neighborhood and Partnership Instrument by €350 million (to a total of €600 million) for all EaP countries, for the period 2010-2013. The bulk of this increase is destined for the CIB, leaving the multilateral component of the EaP underfinanced, and further weakening its relevancy for the countries in question. It has yet to be decided how these resources will be distributed among the EaP countries. Ukraine is expected to receive an additional €25 million annually.

Ukraine's perseverance in collaboration within the EaP framework may be dampened by the lack of a concrete goal in the form of membership perspective. This, however, is both an advantage and a setback for the EaP. On the one hand, the lack of formal membership perspective can be a disappointment, especially for Ukraine, which is relatively enthusiastic (though not very active) about Europeanization and integration with the EU. On the other, membership perspective is not ruled out, allowing the EU to use it as leverage for reform. This is based on the EaP's principles of condition and diversification. Bilateral relations can be developed to varying degrees. Countries that demonstrate greater initiative and will to integrate with the EU through the EaP can do so.

One of the main advantages of the EaP is its flexibility. This ability to adapt its strategic focus in accordances to national and regional developments may allow it to overcome its organizational and financial weaknesses, and focus on the most important issues. In particular, the bilateral component should be strengthened, due to its dominant position as a tool for europeanization. However, it will demand significant efforts from both Ukraine and the EU to produce visible results. Without increased resources (both financial and institutional) from the EU, and political determination for reform on behalf of the Ukrainian side, the EaP runs the risk of becoming a lost opportunity, or an empty promise.

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¹ For an in-depth discussion on the economic vector of the EaP see Shumylo & Gazizullin (2009).

Selected Areas of Cooperation of the Bilateral and Multilateral Components of the EaP²

Bilateral Cooperation	Multilateral Cooperation
<ul style="list-style-type: none"> ▪ Financial and institutional support for implementation ▪ Economic and regulatory approximation ▪ Deep Free Trade Area development ▪ State-capacity building ▪ Regional approximation and development programs ▪ Governmental aid system reform (development of aid instruments, work group creation and training) ▪ SME support (financing and consultations) ▪ Boundary investment projects 	<ul style="list-style-type: none"> ▪ Promoting good governance and democracy ▪ Liberalization of aviation space ▪ Initiating boundary investment projects ▪ Financing ecological initiatives ▪ Co-financing of cross border projects ▪ Common policy of labor migration ▪ Approximation of regulation policy and standards ▪ Promoting regional social and economic development

² Shumylo, O. & Gazizullin, I. (2009). Economic Vector in the Eastern Partnership and Additional Opportunities for Ukraine. In „EU's Eastern Partnership: Additional Possibilities for European Integration of Ukraine” ed. Vitalii Martyniuk, Ukrainian Center for Independent Political Research

Russian oil on the Baltic Sea

By Bo Österlund

There are more than 250 tankers plying the waters of the Baltic Sea at every point of time. After his retirement from the Finnish Navy Commodore Bo Österlund has mapped out the extent of this traffic, confirming that the Baltic Sea is one of the most important shipping lanes for crude oil.

The Baltic Sea is one of the busiest shipping lanes in the world, counting for some 15 per cent of total seaborne world trade. Annually some 85,000 vessels enter or leave the Baltic Sea through the Danish Sounds or the Kiel Canal, i.e. 230 ships a day.

On the Baltic Sea a total of 33,000 ship movements were recorded east of Gotland in 2008 and 22,000 west of the same island. More than half of the vessels entering or leaving the Baltic Sea start or end their voyage in the Gulf of Finland. In 2008 some 45,000 eastbound and westbound vessels passed the waters south of Hanko, an average of more than 125 vessels a day. Of these vessels 23,000 were freighters, 4,500 passenger vessels or ferries and 6,000 tankers. These figures do not include the traffic across the Gulf of Finland between Helsinki and Tallinn.

Additionally 18,000 ships sails west of Åland and some 1,500 ships through the Archipelago of Turku. It is estimated that there are 1,500 vessels underway on the Baltic Sea at every point of time, comprising about 260 tankers, 900 dry cargo vessels, and 200 passenger vessels.

On the Gulf of Finland there are, depending on the time of year, always 400 to 500 ships underway, and about 20 of these are tankers.

Annually an amount of approximately 100 million tons of oil is carried by some 1,000 tankers from the ports at the eastern Gulf of Finland. Off Tallinn the annual volume has already increased to 140 million tons, and 3,300 tankers. The westernmost part of the Gulf of Finland is annually passed by 3,400 fully or partially loaded tankers. The total number of oil carriers on the Baltic Sea, either loaded or en route to a loading port, reaches 6,000.

The economic significance of the Baltic Sea has increased after the turmoil in the early 1990's, affecting Russia and the other coastal nations. As the countries of the former Warsaw Pact introduced market economy, their fast economic growth and the change in the direction of trade from east to west, as well as the significant growth of the foreign trade have increased the traffic across the Baltic Sea.

According to the statistics in the Baltic Port List 2007, published by the Centre for Maritime Studies of the Turku University, 820 million tons of cargo were conveyed on the Baltic Sea; of these more than 320 million tons, i.e. almost 40 per cent, are liquid bulk, mainly crude oil and oil products. The Ministry of Transport and Communications in Finland estimates that the shipments within the Baltic Sea will grow by 60 per cent until 2020. Imports from other areas to the Baltic Sea are estimated to grow by 30 per cent, and export from the Baltic Sea to other areas by 60 per cent.

How much the oil shipments will increase depends to a great extent, on the development of Russian oil and gas pipelines as well as the possibilities of the ports' to increase their capacity in the number of shipments.

Oil production of Russia is based upon its production facilities which are a legacy of the Soviet Union. The exploitation of the natural resources fell dramatically by the disintegration of the Soviet Union, from an annual production of more than 500 million tons to 300 million tons. Rearrangements related to the oil and gas pipelines through Europe, as well as the procedures of securing and rerouting have again increased the oil production to some 450 million tons annually.

As a result of the economic crisis in Russia at the beginning of the 1990's, the oil export was increased to ensure the inflow of foreign currencies. This was achieved mainly by using pipelines, railroad and road transports, and shipment through ports in the Baltic States.

After these rearrangements Ventspils in Lithuania became the largest port for Russian oil export after Novorossiysk in the Black

Sea. Russia also boosted its export over Tallinn, Klaipeda and the new Lithuanian oil terminal Butinge. At the same time, the importance of Kaliningrad as an export port decreased. The booming transit shipments brought prosperity to the Baltic States. Russia was not, however pleased with their way to manage their relations to Russia, and the transit fees were regarded too high. Therefore Russia decided to expand its own existing ports and also to build new ones, above all in the easternmost part of Gulf of Finland. In 2001 President Vladimir Putin inaugurated the new oil terminal in Primorsk, which was connected to the Baltic Pipeline System, bringing oil from the East. Ust-Luga was established as a ro-ro and container port, and it is now being expanded with an oil terminal.

When it became possible to increase the export volumes through Primorsk, the oil pipeline to Ventspils was closed down in the following year 2002. The Russian oil company Yukos has after that started oil shipments to the port by rail. After this new alteration of course, the idea of building a gas pipeline on the seabed from Vyborg to Germany came up as soon as in 2003 according to Swedish sources. The idea was based upon an existing plan originating from a Finnish-Russian joint venture North Transgas Oy in the late 1990's. Even then it was realized that Central Europa would need more gas to ensure its future demand of energy.

Today Russia counts for ten per cent of the oil deliveries to the world market and stands second after Saudi Arabia as an oil-exporting country. In 2007 Russia's crude oil export totalled 220 million tons – 4.4 million barrels a day. In addition to that, Russia exported more than 100 million tons of oil products. More than 50 per cent of Russia's crude oil export is shipped on the Baltic Sea or to the countries by the Baltic Sea. The infrastructure of this export is sustained by the Northern arm of the Druzhba pipeline, leading to Poland and Germany, as well as the oil terminal in Primorsk by the Gulf of Finland.

Finland, Sweden, Germany, Poland and the Baltic States were in 2006 almost totally – up to 95 per cent – dependent on imported oil. Finland imports more than 75 per cent of its crude oil from Russia, the rest from Denmark, Norway and the UK. Germany imports 35 per cent of the oil it needs from Russia. The strategic role of the Baltic Sea as a shipping lane for Russian oil is indisputable.

The port of Primorsk is the most important for Finland's imports of oil. Today there are four, or five, loading piers for up to 150,000 dwt crude oil carriers as well as 18 oil storage tanks with a capacity of 50,000 tons of crude oil each. The annual capacity of the pipeline is 75 million tons. The volume may be temporarily increased by 25 per cent by adding compounds accelerating the flow and decreasing the friction. In last August an amount of 6.6 million tons of crude oil was handled in the port. Every month an average of 60 to 62 loaded tankers leave the terminal, making a total of 750 ships a year, carrying 75 million tons of crude oil. More than 60 per cent of these shipments go to the Netherlands and 16 per cent to Finland.

The new pipeline which is planned to Ust-Luga will have an annual capacity of 50 million tons when it is completed in 2013. It is estimated that it will not increase the total volumes, as it is believed to end the railway shipments to Tallinn. The Port Director of Ust-Luga Maxim Shirokov predicts that the other exports thru the port will increase to 170 million tons by the year 2015, which is almost twice the volume of total seaborne trade Finland.

Bo Österlund

Commodore (ret)

Finland

The role of the Arctic in Russian energy strategy in Europe

By Jakub M. Godzimirski

Over the past few years, Russia has gone through a period of both high expectations and sobering experience of the global economic crisis, revealing the failure of the strategy of economic development propounded by its ruling elite. This experience is like to force the elite to rethink and partly reformulate goals of the long-term strategy for the country's development and may have impact on the realization of several strategic projects, also in the sphere of energy.

National self-confidence soared to unprecedented heights in summer 2007 when the Russian flag was planted by the Russian expedition at the North Pole. This stunt of Artur Chilingarov was widely seen as a highly symbolic proof that Russia was returning as a great power with not only regional but also global ambitions. This move was combined with the semi-official Russian discourse on the country as an indispensable energy superpower and with a growing focus on building a Russian version of what was labelled 'sovereign democracy' intended to make Russia immune to external pressures.

In fact, there are not only symbolic but also other, more down-to-earth reasons why Russia has been paying increased attention to developments in the Arctic. One of those concerns the energy resources believed to be located in this area. According to the last estimates issued by the USGS, 'the mean undiscovered, conventional, technically recoverable petroleum resources in the Barents Sea Shelf are estimated to be more than 76 billion barrels of oil equivalent, which includes approximately 11 billion barrels of crude oil, 380 trillion cubic feet of natural gas, and 2 billion barrels of natural gas liquids'.¹ Those figures make clear how high the energy stakes are and why Russia has again chosen to face the Arctic challenge. This also explains why Russia will have to 'go Arctic' in order to be able to realize its ambitious strategic energy projects.

Some of these projects are especially vulnerable to what will happen in the Arctic, and the most exposed is definitely the Nord Stream gas pipeline. According to official plans, this pipeline will provide Germany and the rest of Europe with up to 55 bcm of natural gas. Half of this volume is to come from the Yuzhnorusskoye gas field, currently being developed by a consortium of Russian and German companies. The other half is to be shipped, starting from 2013, from the Shtokman gas field, the world's second biggest offshore gas field, with 3 800 bcm of gas reserves, to be developed jointly by Gazprom, Total and Statoil. However, it seems that the development of this field may be in grave peril.

Several factors may make the project non-viable. Until recently, it might have appeared that the main obstacles could be of a geopolitical nature, as there was strong opposition in some EU countries to the construction of the Nord Stream pipeline needed to transport gas from Shtokman to West European markets. The recent decisions of the Danish, Swedish and Finnish governments to allow Nord Stream to go through those three countries' exclusive economic zones seem to have removed this obstacle, as the remaining two governments that have to approve the project are those of Germany and Russia, and this seems to be a mere formality.

However, other, perhaps more serious, dangers now seem to loom. The fact that the companies involved in development of the Shtokman field decided to postpone the final decision to 2010 may mean that the purely technological

challenges may be greater than originally expected.² Another important factor is the uncertainty linked to the future development of oil and gas prices. In 2008, with the oil price hitting first the magic \$100 per barrel mark and then skyrocketing to almost \$150, it could seem that the project that was to send until 70 bcm of gas to European and global gas markets could become an effective money-making machine, and that technological solutions would be found, whatever the cost. Calculations based on the average gas price in 2008 (\$410 per 1000 m³) showed that the project could generate as much as \$30 billion revenue per year – but then came the dramatic drop in oil prices, to \$30 per barrel in December 2008, demonstrating the massive price volatility and the impossibility of making reliable short-, mid- and long-term calculations of the commercial viability of such projects.

The economic crisis has also resulted in a significant drop in demand for Russian gas in Europe, forcing Gazprom to reduce its gas production.³ This lessened Gazprom's revenues, which were already suffering from the lower gas price on the European gas market, and forced the company to announce cuts in its ambitious investment programme.⁴ Due to the lack of infrastructure, the surplus of gas cannot be shipped to other markets – like the Chinese – to compensate for the fall in European demand. As Russia has no LNG facilities near fields that produce gas for the European market, that option could not be used either. The global LNG market also seems affected by two recent developments – the current economic crisis, and – perhaps even more important in the long run – the increasing production of non-conventional shale gas in the USA, which should substantially reduce the US demand for LNG. As part of the gas from Shtokman was to be sent to the USA as LNG, this might also have negative implications for that project.

The last factor involved is the Gazprom's decision to cut its investments programme. True enough, Prime Minister Putin has announced that those cuts will not affect the development of the gas sector in Russia.⁵ All the same, this may lead Gazprom to focus less on the challenging Shtokman field and to concentrate instead on the Yamal Peninsula, from which gas could be transported not only to Europe but also to China, as announced by Putin during his recent visit to Beijing. Such a change of focus could jeopardise the realisation of the Nord Stream: there simply might not be the gas to fill that planned pipeline.

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² The problems faced by Statoil in the Snøhvit field clearly illustrate how challenging technologically similar projects may be. For details on the latest developments there see <http://e24.no/boers-og-finans/article3387391.ece>

³ <http://www.reuters.com/article/rbssEnergyNews/idUSLU3329520090930>

⁴ <http://lenta.ru/news/2009/09/03/gazprom/>

⁵ <http://lenta.ru/news/2009/07/13/cut1/>

¹ <http://pubs.usgs.gov/fs/2009/3037/pdf/FS09-3037.pdf>

Prospects and consequences of START follow-on treaty

By Bartosz Cichocki

Presidents Obama and Medvedev have probably signed a Strategic Arms Reduction Treaty (START) follow-on agreement shortly before this paper was published. At least both leaders have repeatedly confirmed their intention to wrap up negotiations before December 5, 2009 – when the 1991 US-Soviet nuclear agreement was set to expire – since the bilateral meeting on the eve of the London G20 summit on April 1, 2009.

On July 6, 2009, the US and Russia agreed, that the future treaty will cut their nuclear arsenals to 1,500-1,675 operational warheads and 500-1,100 delivery vehicles (heavy bombers, deployed intercontinental ballistic missiles and their launchers, deployed submarine-launched ballistic missiles and their launchers). Currently, the US has about 2,200 operationally deployed warheads and Russia – about 2,800. Both sides are already within the above mentioned boundaries for delivery vehicles – closer to the higher one in case of the US and to the lower one in case of Russia [1].

However, the negotiating parties remained far apart on a number of issues. Experts point out the following controversies as most significant: i) rules for counting warheads and delivery vehicles; ii) downloading provisions to allow the parties to remove warheads from the delivery vehicles and to count downloaded missiles with fewer warheads (and with fewer missiles in case of downloaded submarines); iii) measures to prevent rapid uploading of downloaded systems (so called breakout potential); iv) conversion of some START-accountable ballistic missiles to conventional-only roles and removing them from being accountable under the new treaty; v) monitoring and verification measures; vi) whether to bring limits to missile defenses into the treaty on strategic offensive weapons [2].

How these issues have been solved (and whether they actually have been solved) is critical to evaluation of the consequences of a START follow-on treaty. In such cases Sherlock Holmes used to say: it is a capital mistake to theorise before you have all of the evidence. Some general conclusions seem, however, unquestionable.

Firstly, reaching a compromise on all the controversies in such a limited time frame would make a spectacular diplomatic success. It has taken almost a decade for the US and Soviet Union to agree on some hundreds of pages long START in 1991, more than five years to conclude Intermediate Nuclear Forces Treaty (INF) negotiations in 1987 and six months to sign two pages long Strategic Offensive Reduction Treaty (SORT aka Moscow Treaty) of 2002. And still, a START follow-on treaty remains to be ratified by the parliaments, which may take months and become subject of political dispute in US Senate (depending on the content of agreement) and/or hostage to a wider US-Russian security agenda in Duma. That was the case with START II – signed, but not ratified in Russia and ultimately denounced by Moscow, following the US withdrawal from Anti-Ballistic Missile Treaty (ABM) in 2002.

Secondly, regarding security concerns of Central and East European states, whenever the US and Russia reached a strategic agreement or understanding, it made Moscow less inclined to use confrontational approach in her policy toward the neighbors and thus contributed to regional stability. President Clinton's engagement with president Yeltsin helped the 1999 NATO enlargement to become a relatively conciliatory undertaking with regard to Russia's response. President G.W. Bush's look into president Putin's soul (followed by strategic arms treaty offer, understanding of the Kremlin's Chechnya policy, launch of the Russia-NATO

Council, Russia chairing G8, etc.) resulted in Russia's tolerance to the Baltic States acceptance to NATO in 2004 and Ukraine's, Georgia's approximation with the Alliance. And the other way around. Whenever the US ignored Russia's concerns in security area (ABM abrogation, Iraqi operation, Missile Defense offer for Central Europe, US military presence in Central Asia, etc.), it provoked the Kremlin to use energy blackmail and military threat against its former colonies and satellites [3].

Thirdly, the above does not have to constitute a rule. For Russia does not feel a weak side anymore and defines Central and East European gains as her own failures. Additionally, Russia does not seem to be impressed with president Obama's Global Zero vision and regards a START follow-on treaty purely as an instrument to regain two decades gone parity with the US. As the Soviet style and scale Russian-Belarusian military exercise "West-2009" showed this September, Obama-Medvedev strategic dialogue is yet to be accompanied by the rapprochement in Russia's relations with her neighbors. And the latter should be regarded a necessary element (and not a bargain chip), as far as rebuilding of confidence in US-Russian relations is concerned.

Fourthly and finally, for a START follow-on treaty to produce tangible effects in both transatlantic and Central-East European security, it should be followed by arrangements concerning Russian tactical nuclear arsenals and conventional weapons [4]. Today, importance of both in Russia's security policy is rising to a detriment of the former Soviet and Central European space stability.

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Please, note: the views expressed herein are those of the author and do not necessarily reflect position of the NSB.

Travelling by sea has a bright future

By Andres Hunt

Baltic Sea offers a magnificent and unique sea landscape, which has been discovered by numerous passenger shipping companies operating here.

The passenger shipping market has grown by millions of passengers in past years, from 13 million to over 17 million passengers annually on the northern part of the Baltic Sea. Tallink started with 160 000 passengers in 1990 and reached over 8 million serviced passengers in the fiscal year of 2008/2009. In addition to the picturesque Baltic Sea, what attracts people to travel by sea?

The attitude towards travelling in general has changed much during the past 10-20 years. The same trends are also visible in other transportation sectors. People evaluate the time and especially free time very highly. We could name the new trend with the term "effective travelling". Quick, comfortable and all-inclusive trips are very popular. All inclusive does not mean the usual hotel accommodation in this sense, but the variety of travel experience during one trip.

It starts with booking the trip. Tallink has invested into modern and effective online booking system. It is a win-win situation, since passengers can book their ferry tickets, meals, accommodation and even excursions in one place at once. The company on the other hand has lower costs in personnel and offices.

During the years, also the understanding about passenger ships has changed. The passenger ferries built in 1980-ies are quite different from the modern ones.

Nowadays, by sea travel one of the most important aspects is to have a comfortable and multifunctional vessel. The passengers of cruise lines are especially interested in having a selection of shops, restaurants and entertainment facilities on board. It is again the all-inclusive option, as during a cruise of only one to two days, people can enjoy everything necessary for a great mini-vacation in one place, on one ship. Tallink has invested over 1 billion Euros into building new generation cruise ferries for the routes on the Baltic Sea. The market demand is there and the passenger numbers show a positive correlation with the new buildings set to the routes. Tallink always tries to be one step ahead of the market and tries to discover the new market trends in advance. Therefore it is possible, that in the future there are additional changes to the route's concepts or the fleet as they both are linked to the travel market developments in general.

A good example of effective travelling and passenger shipping innovation is Tallink Shuttle concept. Tallinn-Helsinki shipping route is one of the busiest international shipping routes in the world. Today, Tallink services almost 3, 5 million passengers annually on this specific route. 5 years ago the demand was growing, but the possibilities were different. Tallink had up to 6 vessels on the route, from which the 4 high speed crafts were highly weather sensitive and had a low capacity of passenger vehicles. Cargo capacity of these vessels was almost zero; therefore the larger cruise ferries and special cargo ships had to do this work additionally. When Estonia became the member of EU

and the employment policy enabled Estonians to go to work to Finland quite easily, the demand on the route grew even faster. Demand for short vacations both ways was there, the demand for a vacation with a personal car was also rising. Tallink ordered 2 new generation high speed ferries with the capacity of almost 2000 passengers and 2000 lane meters of car deck (450 passenger vehicles). To enable the travelling between 2 capitals all year round, a high ice class is also necessary. The two vessels operate now under the concept Tallink Shuttle and are appreciated by the passengers by their flexible and frequent time schedule, all year round traffic and large space for cars. They are the most booked ferries of the 19 vessels the group owns. It saves time and money of our passengers, diminishes the environmental impact and fuel costs of the company.

When the concepts of the cruise ferries are similar to the ones with cruise ships, the difference lies within the duration of the trip. As there is a clear trend towards shorter, but more effective vacation trips, the short cruises are especially popular in the region.

Especially during the times of economical recession the short cruises are favoured due to the travel expenses. While the ships enable to experience various cuisines, beautiful nature, spa treatments, shopping etc, the travel costs are lower compared to the flight travel, where you additionally also have to book a hotel for an overnight stay. So sea travel can be also seen as cost effective.

During last 10-20 years, also the possibilities to travel to neighbouring countries have widened a lot. The effectiveness is also seen here – no more border control (Schengen area), no more visas, no more documents to be filled. It is easy and comfortable.

People are more than ever interested in travelling to nearer countries; many of those are brand new travel destinations. The Baltic countries for instance are a popular travel destination for people from Nordic countries. Baltic countries have a rich history, architecture, nature and are suitable also for lower budget travelling.

Also the environmental aspects are not to oversee. The shipping is environmentally friendly way of transportation. It is essential to know and develop this advantage for instance by investing to the fleet. In general, passenger shipping in terms of Tallink is all inclusive – environmentally friendly, cost and time efficient and attractive vacation environment. This is the demand today. But we keep our eyes open about tomorrow as well.

Andres Hunt

*Vice Chairman of the
Management Board*

AS Tallink Grupp

Estonia



Russia takes action towards ecological future

By Pekko Kohonen

I have travelled extensively in Russia, touring towns and cities from east to west and north to south. The very warm welcome I have received everywhere could be attributed to the driver of our company ideology: to convert discarded material into new, valuable raw material, and to ensure a clean environment for everyone. No municipal manager wants to waste these valuable resources; instead, they want their region to be as ecological as possible. The first and most significant element required for change already exists – ‘will’. Without the will of private and corporate citizens and decision-makers, nothing can ever change.

‘Must’ is another effective driver of change, but when combined with will it becomes even more potent. Even today, the Soviet legacy still dominates many of Russia’s infrastructure solutions. But back in the Soviet days, the strain on infrastructure was smaller, and needs were very different, as were consumer habits and consumer behaviour. The amount of waste generated by consumers was much smaller, and industry had a practically endless supply of raw material which meant product life cycle was never really a consideration.

But following the emergence of private ownership, a real pricing system and global economy in Russia, things will inevitably have to change. Companies and municipalities will come face to face with the necessity of change as landfills fill up, and companies will no longer be able to afford to ignore the financial value of their raw materials and industrial by-product flows. Russia still remains a closed economy to some extent, which means the real power of ecologic force has not yet dawned on local players. Meanwhile, in the European markets, companies have long been forced to fulfil certain eco-requirements in their production operations, if they wish to succeed. Russian companies seeking access to the global markets have already felt this kind of a ‘must’.

Municipal directors admit this development, and they have the will to change things. What many towns and cities lack is **faith**. City and town leaders know that they will have to change the way things are done, but they blame everything on the “large soul” of the Russian people. People throw litter on the streets if the waste bin is too far away, or forget the regulations they are expected to comply with. It has been said that the Russian people are not systematic and obedient like the Scandinavians, which is why changes such as sorting-based recycling are impossible to implement. They say this is easy for us Finns, but that for the residents of their home towns and cities it is completely or, at least, almost impossible. What these town fathers forget is that the recycling system currently in place in Central Europe and Scandinavia did not appear overnight; the system took 40 long and sometimes painful years to develop, and is still not ready.

Personally, I would be inclined to give more credit to the “large soul” of the Russians, which is inherently closer to nature and green values than, say, the more technocratic Scandinavian soul. Traditional soft values such as friends and family, enjoying life and enjoying the natural environment are very important to Russian people. The Russian soul simply thrives in clean nature, sitting by the water with friends, enjoying shashlik and hand-picked mushrooms or local vegetables bought at the local store. Russians want to have all of this and are prepared to make sacrifices. Russians should be provided with an opportunity for pro-environmental action.

When we have faith that we can make a difference, the only missing element is **actions** that will enable us to pursue our common goal.

This requires a significant change in the current infrastructure to enable a more ecological approach. People should be encouraged and motivated financially to act in a more eco-conscious way. Sometimes people and companies may lack the will to make things happen, and that’s where the ‘must’ mentioned earlier enters the picture. ‘Must’ was necessary in the EU, too, despite a strong will to do what’s right. It was not until legislation introduced the ‘must’ that people started to act in accordance with their will to change. Supporting this through legislation is what Russia needs as well. In Russia, highly centralised power enables quick legislative changes that could promote an environmentally sound future.

Back in the Soviet era, everything could be ordered from the top down, but the lesson learned from history is that this is not always the best way of organising things. Promoting environmental awareness in Russia is everyone’s concern, and everyone should play their part in achieving this goal. Fortunately, it appears that more and more is happening on this front:

- Cities are showing an interest in municipal environmental management.
- The media is showing an interest in the subject.
- Russian companies are starting to buy environmental services.
- People appreciate clean yards and clean environments.

Even President D.A. Medvedev named environmental awareness one of Russia’s key priorities in his speech in January 2008. In this speech, he also urged organisations to take action to launch the recycling industry in Russia, in response to which environmental enterprises operating in Russia established the Russian Association of Waste Recycling (Ассоциация Рециклинга Отходов, АРО). This association has already initiated talks with the federal and regional ministries on development opportunities in the recycling sector.

Co-operation between various fields, such as government administration, companies and private consumers, is required to build a more ecological Russia. It’s time to roll up our sleeves and get to work. The first step could be to follow the EU’s example and enforce a landfill tax, which would raise the price of landfill waste and encourage people to recycle.

Let’s give our souls a chance.

Pekko Kohonen

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The Baltic recovery – anything else but a long hard slog?

By Ralf Wiegert

Once Europe's leader, now the laggard – the Baltic region has gone through extremes during the last three years. A region that has benefited enormously from European Union (EU) membership, both in terms of trade as well as investment inflow, has been caught wrong-footed as the global crisis fully struck in the second half of 2008. Already sliding into recession following several years of neck-breaking growth, the global crisis has severely aggravated the looming landing of the Baltic tigers in 2008 and 2009. More than once during the last 12 months, it even looked as though the collapse of Latvia's euro-based exchange-rate peg could trigger a pan-central European financial crisis, with repercussions for western Europe as well.

A region-wide disaster has been averted, not least thanks to financial support from the EU, the IMF, and other international lenders. The economic situation has evidently stabilised both in Central Europe and the Baltic region. With the Baltic countries' budget plans for 2010 being close to final endorsement, the fiscal outlook has become more certain, injecting a crucial amount of stability to the markets. Latvia's multinational loan programme will most likely be maintained after the government has adopted yet another round of harsh fiscal austerity measures. Meanwhile, as was recently remarked by EU Economic and Monetary Affairs Commissioner Joaquin Almunia, Estonia is currently on track to secure euro adoption for January 2011, a step that would further enhance stability in the region and improve chances for a recovery.

Against the backdrop of the abysmal first half of 2009, all of that is clearly good news for the Baltic region. However, being confronted with a weak outlook for the next two years, the fact that the downturn has halted after all is scant consolation: the output gap remains large, unemployment is still rising, and the strength of the euro makes it difficult for the Baltic trio - Estonia, Latvia, and Lithuania - to benefit from the visibly improving European outlook.

Meanwhile, a credit crunch has gripped the Baltic countries. Banks have been adamant to scale down their exposure, while households and companies alike are reducing their debt level and saving more. Although the scale of the debt problem varies from Latvia, to Estonia, and eventually Lithuania, the ramifications for the economy are the same. Domestic demand will remain weak for at least three to four years. All three economies will eventually start to grow again in 2011 at the latest, but it will take until 2015 (in Estonia's and Lithuania's case) and 2018 (in Latvia's case) before the pre-crisis level in private consumption will have been reached again, according to IHS Global Insight's forecast.

Because exports are recovering earlier, GDP in the Baltic countries will climb back to the pre-crisis level around 2014-16. At that point, around eight years will have been lost since the start of the recession, making the current downturn comparable to the savage reduction of output following independence from the Soviet Union and the abolition of central planning. Furthermore, it is hardly realistic that the pre-crisis output level in 2015-16 will be produced with the same job count as in 2007-08. High unemployment - in Latvia's case, extremely high unemployment, with rates close to 20% - is likely to remain a constant feature for the coming several years. It will not only slow down the economic recovery, but also alter the way of policymaking, especially in Latvia, where the populist, social-spending streak could gather strength.

There are still chances that unemployment could be reduced more quickly, but this largely depends on foreign capital and the investment climate in the Baltic region in general. The majority of unemployed are well-skilled and have on-the-job experience; meanwhile, the wage level in the Baltic countries, especially in Latvia and Lithuania, is still very low compared with Western Europe. According to Eurostat, average total personnel costs per employee have varied between 17% (in Lithuania and Latvia) and 25% (in Estonia) of Germany's cost level in 2006. Cheap skilled labour makes the region still attractive, but the advantage may be discounted by a further postponement of euro adoption.

Indeed, if Estonia secures the euro for 2011, it will be a major boon for the smallest economy of the Baltic trio. All depends on whether the government keeps the fiscal deficit below 3% of GDP. The government and the Bank of Estonia are sounding increasingly confident, as apparently does the EU Commission, yet so far the issue remains balanced on a knife's edge.

Latvia and Lithuania are much less lucky, having to pay now for their fiscal sins of the recent past. Although fiscal spending has already been curbed savagely, further belt-tightening will be necessary during 2010-13, in order to balance out public-sector finances and prepare for euro adoption, which is not likely to be possible before 2015, or 2014 at the earliest. That being said, Estonia could eventually emerge from the crisis as weakened but clearly stronger and even more prosperous compared with Latvia and Lithuania.

Moreover, if the European Council invites Estonia to join the Eurozone in 2010 and announces the final conversion rate for the kroon, devaluation talk will finally be put to rest – at least as far as Estonia is concerned. In theory, Estonia could still devalue the kroon by up to 15% against the euro and join nonetheless, but this seems a fairly remote scenario.

Regarding Latvia and Lithuania, a devaluation of the lats and the litas, respectively, is unlikely for the next 12 months, at least if the budget plans and tax amendments for 2010 are eventually passed by the countries' parliaments in December. A one-off devaluation could become an issue again, though, at some later stage. Indeed, as the fiscal situation will defer euro adoption until at least 2014, a devaluation could be pushed through by mid-2011 without harming euro chances.

Central Europe's financial markets will have stabilised further and written down most of the region's losses by then. Indeed, Scandinavian banks operating in the Baltic region have had enough time to brace themselves for an even worse outcome, including a steep devaluation. If Europe's recovery is in full swing by the end of 2010, and Latvia and Lithuania are still lagging, the temptation to devalue the lats or the litas to kick-start the economy might be too strong for Latvia's and Lithuania's authorities, whoever is in office.

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Building innovation economy in Russia – big ambitions are build by small steps

By Peter Zashev

Everybody who follows regularly the political and economic development in Russia is aware how high in the agenda are such topics as innovations and modernization of the economy. Both Russian Prime Minister and President spoke numerous times about the need to diversify the economy and diminish its humiliating dependence on exporting raw materials, chiefly oil and gas.

That very topic was also at the heart of the President Dmitry Medvedev recent address to the Federal assembly. It seems that there are two substantial problems in achieving these fine objectives. One is that, as history teaches is, the grand vision of the Russian federal authorities often does not match the interests of those that must implement it. The other seems to be in the inability of many Russian policy makers to break a grand vision in a list of concrete small tasks that may sound less grand and breathtaking but are more prone on tangible results.

Innovations can not materialize by a top down issued instruction. Down at the bottom in the real economy there must be scientists and companies finding common interests to cooperate and do something together. The present organizational setup is not inductive for the two parts to seek and develop such cooperation. Instead both sides prefer to wait for the government to offer some form of grant or subsidy etc. This is easy to fix. Building joint projects with companies, raising (partial) financing for projects from the companies should be part of the regular evaluation criteria for universities, research institutes and researchers. This is one example for a small step that has large tangible impact. Equally important is to offer companies some incentives for more actively using the knowledge, skills and available capabilities of universities and research institutes. There are many different alternatives from simple tax breaks on money invested in such R&D projects to more elaborated schemes when the each rouble invested in R&D could be supported by another one paid by the government. To fire up the cooperation between industry and academia should be a top priority.

Instead it seems the government prefers to apply centralized schemes in the form of mega-projects, special economic zones, techno parks etc. Naturally they all have their place and importance. However none of them addresses directly the above described central weakness: industry and academia do not cooperate enough. On the top of it such cooperation will not mean much in the absence for a market for the new products being born, which requires skills and knowledge in commercialization of innovations. For all its size and pre-crisis economic growth rate the Russian market alone is often not big enough for gaining critical sales for new products and technologies. Fortunately in modern times markets are global for those being skilled in international entrepreneurship and marketing etc. Unfortunately at present the Russian way of innovating and commercializing seems to be mostly domestically oriented.

Russian policy makers seem to put their faith in grand projects! Take the nanotechnologies where the main operator is little controlled State Corporation with sizeable financial opportunities. Besides number of Russian cities and

regions setting up their own nanotechnologies centres (doing what!?) it is not clear what are the results so far. At a recent strategists forum in Saint Petersburg the regional authorities together with big names as Finance Minister Kudrin were talking as some kind of a mantra the words of “proryv” (breakthrough) and “nanotechnologies”. The logic perhaps is that what is needed is grand concentrated efforts in one given field leading to breakthroughs.

However the experience of many countries will show that modernization and progress in innovations is gradual process that consists of many small steps in which often nothing grand or revolutionary happens. Although innovative activity is often linked with high technology sectors of the economy, companies in low- and medium technology sectors also innovate, and such innovations are important for the general level of national competitiveness. These companies may innovate in the field of production processes but also organisational and marketing innovations. Russia has plenty of wood. Producing nice design sauna accessories and marketing them to the world as an expensive brand is pure innovation even if it does not sound like launching a satellite. In that respect it may be very useful for many Russian regions to concentrate on what they have and what they may develop with some more simple but more needed innovations and improvements instead of spending their little resources on yet another nanotechnologies centre or techno park.

It is the every day small steps and actions of individuals that achieve the great things. For that to happen the government only needs to send the right signals in the form of concrete incentives and evaluation criteria that aim at results that may be described in qualitative and quantitative terms. As far as the central government believes that it may be simultaneously the main initiator, financier and often user of innovations the other players in the innovation system will deliberately chose to stay idle. Regional authorities will produce (or rather fake) grand innovation initiatives of the type they know pleases most central government. Companies will wait to get and use a state order or money instead of investing in new markets, products and innovations. Academia will continue to complain about inadequate funding for projects that are anyway of little interest to companies. That will be a pity end for the President's sincere wish for modernization!

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Belarus and its economic relations with the countries in the Baltic Sea Region

By Irina Yeremeyeva

Belarus has significant economic ties with the countries of the Baltic Sea region. This country plays an important role in the transfer of traded goods from East to West, from North to South. Among the five major trade partners of Belarus three belong to the Baltic Sea region. They are Russia, Germany and Poland.

Russia plays a significant role in Belarusian economic development and the impact of Russia on Belarusian economy is very high. The best indicator of this is the status of their trade. The structure of export-import of the Republic of Belarus with Russia was 47.2% of the whole trade turnover volume in 2008. Exporting food to Russia has been one of Belarus' most important and reliable trade sectors. In 2008, Russia bought 93% of Belarusian meat and dairy products. And Russia always uses this instrument in its political and economic struggle. This country has a tradition of banning goods from neighboring countries of the first sign of disagreement, like the 2005 ban of Polish meat, the 2006-2007 ban of Georgian and Moldavian wine, the 2009 ban of Belarusian milk. And for a while Russia has got everything it wants. And the second way of impact is a price of Russian oil and gas for Belarus. But since 2007, the economic relationship between Russia and Belarus has been steadily worsening, when Russia raised gas prices and demanded that Belarus give up control of gas transit from Russia to Europe — about 20% of Russian gas exports to Europe go through Belarus, and so Russia wants to take over Beltransgaz, the state-run operator of Belarus' gas-pipeline network. And soon this instrument will not work anymore.

Germany is Belarus' second most important Baltic Sea region trading partner. In 2008, the volume of bilateral trade increased by 24 per cent compared with the previous year, to USD 3.61 billion. Belarus' principal exports to Germany are textiles, wood and wood products, medical equipment, chemical products, tractors and optical products. The main imports are capital goods, machinery and equipment, chemical products and motor vehicles. Despite continuing economic and administrative difficulties, 338 German companies are currently operating in Belarus including 189 joint ventures and 149 foreign companies. Six Belarusian companies have offices in Germany. These are Minsk Tractor Works (Belimpex Handels GmbH in Leipzig), Belarusian Steel Works (Belastahl Aussenhandel GmbH in Berlin), Belmagistralavtotrans (Belmagistralavtotrans Spedition GmbH in Alzey), the national air company Belavia (Frankfurt am Main), the Belarusian Chamber of Commerce and Industry (Leipzig), Belneftekhim Concern, and Belarusbank (Frankfurt am Main).

Credit and investment cooperation plays an important role in the Belarusian-German economic relations. Since 1992 Germany has extended more than USD 550 million in loans to Belarusian companies. In 2008 Belarus attracted USD 116.8 million of German investments, including USD 93.7 million of direct investment.

Poland is the third trade main partner of Belarus in the Baltic Sea region. In 2008 the Belarusian-Polish trade was up by 44.9% to USD 2.96 billion. Export to Poland reached USD 1.8 billion, import USD 1.2 billion. The increase in Belarusian export was due to the growth in the deliveries of oil products, liquefied gas, crude oil, potash fertilizer, electricity, timer, tractors. In 2008 Belarus launched exports of 106 new commodities to Poland.

Speaking about the Belarus-Polish investment cooperation, Polish investors are still too cautious in the questions of investment in Belarus. Since 2002 the Polish investments have summed up to about 200 million USD. 400 enterprises with Polish capital are registered in Belarus. Poland is not on the list of the countries leading investors, it's because Poland doesn't have enough free capital to invest, and this country needs investment itself.

Belarus also has good economic relations with such Baltic Sea region countries, as Lithuania and Latvia. In September 2009 trade turnover between Belarus and Lithuania exceeds USD 1 billion. 500

goods items are exported to Lithuania: from products of petrochemical complex to building materials. One of the most active avenues of cooperation is transportation of goods through Klaipėda port. Also, Lithuanian businessmen plan to invest about EUR 1.5 billion to the Belarusian economy. In 2008 318 enterprises with a share of Lithuanian capital were registered in Belarus, including 177 joint ventures and 141 foreign-owned companies. All in all, the investments amounted to USD 43 million, including USD 10.9 million in direct investments. Investment cooperation between Belarus and Lithuania is especially successful in building trade and entertainment facilities as well as hotels and the development of transport and logistics infrastructure (building a trade centre in Minsk by Lithuanian trade company Senukai, building a transportation and logistics terminal by Vingis Logistic Group company, building a trade and entertainment centre in Zhlobin by Belalit company and many others).

In 2008 Belarus-Latvia trade totaled USD 2.32 billion. Belarus exports to Latvia petroleum products, chemicals, carbon, steel semifinished products and rods, tractors. Import from Latvia was dominated by frozen and tinned fish, animal feed, medications, metalware and textiles. Latvia invested nearly USD 600 million in the Belarusian economy in 2002-2008. In 2008 alone despite the crisis Belarus attracted USD 97.7 million in Latvian investments including USD 36 million direct investments. Latvia is an important transit country for Belarusian cargoes, first of all, oil products and potash fertilisers.

The trade and investment cooperation with other Baltic Sea region countries such as Estonia, Finland and Sweden is not developed well. The trade of these countries with Belarus is only about 3 % of total trade and the investments are not so high. But it's really very important for Belarus to develop cooperation with these countries. Baltic Sea countries can help in transferring the positive experience of the Nordic countries to Belarus, especially in developing relations between research and business. Economic cooperation is the most intensive, pragmatic and, certainly, a mutually advantageous direction of the Belarusian-Baltic Sea region relations.

To intensify economic cooperation between Belarus and the Baltic Sea region, it is necessary to settle as soon as possible problems complicating contacts in trade and economic sphere: simplify visa, customs and border-crossing formalities, to modernise and expand a border infrastructure, to develop in every possible way transit opportunities of neighboring countries.

Thus we can draw the conclusion Belarus should focus on further efforts aimed at promoting productive economic co-operation within the Baltic Sea region. The geographical neighborhood pulls together interests of our countries on many strategic directions, including trade, investments, transit and energy. Recently together with Baltic Sea region countries we have reached a high enough level of mutual understanding on these fields. We should keep and increase this common achievement, transforming it into specific projects useful to our countries.

Irina Yeremeyeva

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Belarus



Kaliningrad – unsustainable economy (was growing better and now is decreasing faster)

By Georgy Dykhanov

Financial situation of enterprises

In the I half of 2009 economic conditions in the region evolved significantly worse than in the corresponding period of 2008. Reduced demand for goods and services, reduction of production volumes, rising late payments have led to a deterioration of the financial situation of enterprises, reducing investment activity and their effectiveness. During January-March 2009 the total capital of regional enterprises decreased by 4.1% (January-March 2008 witnessed its growth by 3,7%). In addition, attracted resources decreased by 6,9%.

In the composition of the attracted resources, long-term liabilities increased by 10,4%, while short-term liabilities decreased by 15,4%. As a result of these changes, the debt burden on equity fell slightly - the ratio of own and attracted capital decreased from 1,8 (at 01.01.2009) till 1,7 (at 31.03.2009). In general, the growth of loans in loan form was typical for large enterprises and was determined by long-term debt on loans by 13,2%.

For small, large and medium-sized enterprises total loans and credits in general declined. However, small enterprises in January-March 2009 increased their short-term loans, derived from non-bank organizations, by 10,7%; large and medium-sized enterprises have attracted long-term bank loans, the aggregate volume of which increased by 4,7%. The greatest tenseness of the payments is still characteristic for small enterprises, where 79,3% of all outstanding loans of banks are short-term, the lowest - for the largest enterprises (23,6%).

It should be noted a marked deterioration of payment discipline - for January-March 2009 **overdue payables of enterprises have increased in 2,6 times, overdue accounts receivable - in 1,5 times**. The investment activity of enterprises in the I quarter of 2009, compared with the corresponding period of the last year, has declined, owing to the reduction of all the elements that make up the non-current assets, except for fixed assets, an increase which amounted to 7,6%.

Analysis of the results of the first quarter in the segment of manufacturing industries suggests that the recession over 50% (compared to last year) will not allow companies of the sector to restore old volumes without loss of production, or stop the entire enterprise, such as Techprominvest. The loss of personnel, deteriorating financial situation, leading to the decision to suspend the bank's lending and even a requirement for early repayment, does not allow to hope for a quick exit of enterprises on the pre-crisis level of shipment.

Economic situation

Began in mid-2008 the deteriorating of economic situation in the Kaliningrad Region in January-June 2009 had a tendency to slowing down. This is largely due to the slowing decline in demand for goods and services and to the some improvement in production, as evidenced by a gradual increase in the proportion of enterprises that reporting an increase in output of their goods and services. However, in the 1 half of 2009 compared with the corresponding period last year, under the influence of such negative phenomena as the growth of overdue payables and receivables, the situation has deteriorated significantly with provision of the companies with working capital, has intensified the negative impact of changes in the ruble exchange rate for business activities, essentially increased risks of economic activities.

Against the backdrop of companies' high demand in borrowed funds, credit conditions for the analyzed period have worsened, while their impact on production has increased. Along with this such factors as demanding for products, providing the enterprises with working capital, availability of outstanding receivables increased impact on the main activities of enterprises. In general, most noticeably deteriorated economic situation of such enterprises activities as construction, agriculture, manufacturing of machinery and equipment, production of vehicles and equipment.

Banking sector

The difficulties of the regional economy in crisis affected to the functioning of the banking sector of the Kaliningrad region. Compared with the I half of last year slowed the pace of growth of assets and resource base of credit institutions operating in the region, that resulted in a slowdown in lending. Arrears on loans have significantly increased. The amount of the banks profit reduced as well.

At 01.07.2009 the banking sector of the region consisted of 7 regional banks with 1 branch and 35 branches of nonresident credit organizations, including 4 branches of the Sbergatelniiy Bank of Russia. In comparison with 01.07.2008 the number of regional banks fell by 4. As a result, saturation of the Kaliningrad region by credit institutions amounted to 4.6 per 100 thousand of population, while on 01.07.2008 it was 5,5. At 01.07.2009 the aggregate capital of existing regional banks amounted to 7,4 billion rubles, that on 6,4% more than at the beginning of 2009, but on 10,5% lower than at 01.07.2008.

During the analyzed period, deposits of legal entities in a whole decreased by 0,1% (for the I half of 2008 - growth was in 1,8 times). At the same time, in the departments of Sberbank of Russia and other non-resident subsidiaries of credit institutions funds of legal persons' deposits increased by 10,1% and 2,0% respectively.

Arrears on loans given to the economy of the region (for non-financial organizations and individual entrepreneurs) on 01.07.2009 amounted 70,4 billion rubles (78,3% of total loan debt), increased from early 2009 on 5,8%. In general, the outstanding debt continues to rise, approaching of 10% (in Russia in general - about 6%).

Activity in retail lending in the analyzed period has decreased. At 01.07.2009 arrears on loans given the population in a whole has decreased since the beginning of 2009 to 12,9%, whereas for the same period of the last year saw its growth at 21,9%. The greatest decline (by 19,7%) debts of individuals formed for branch offices of stranger credit institutions.

Against the background of overall decline in lending, arrears grew at a considerable pace. Total arrears on loans given for credit institutions operating in the Kaliningrad region has increased since the beginning of 2009 on 43,3% and its share in total debt has reached 9,1% (on 01.01.2009 - 6,4%). The proportion of arrears on loans to nonfinancial institutions, at 01.07.2009 amounted to 10,3% (at 01.01.2009 it was 7,7%), and for loans to individuals - 6,2% (at 01.01.2009 - 3,4%). It should be noted that the largest proportion of arrears on loans given for the region's economy and individuals at 01.07.2009 was noted in the branches of nonresident banks.

The trend to an increase in accounts payable due to lower shipment lead to deterioration of the situation with supplying of the companies working capital and cash at their

disposal. Provision with contracts also decreased, which further reduced the creditworthiness of the companies, along with falling sales. The negative change in the ruble exchange rate also contributed to a sharp decrease of working capital of most companies, dependent from the supply from abroad, herewith the increase of tariffs of natural monopolies and the growth of rent due to the growth of the cadastral cost of land also contributed to growth in accounts payable.

If we consider the dynamics of the GDP of Russia and the GRP of Kaliningrad region, it is easy to observe that advanced growth of the GRP of the region in previous years are now "compensated" by much more substantial fall in the region's economy on the backdrop of the entire country. Primarily, this paradox is the result of shortsightedness and inconsistent actions of regional authorities in the field of economic policy.

Under such adverse conditions the regional authorities should:

1. Stimulate the demand, reduce the tax burden on households (including cars, real estate), reduce household expenditure (including public utilities, the parent fee and other fees in kindergartens, school levies, sports sections, etc.)

2. Regulate the tariffs of natural monopolies, take antimonopoly actions, where possible - reduce bureaucratic barriers, as the main cause of the growth of transaction costs.
3. Develop a set of measures to attract investment, reduce barriers to new investment and provide support for investment in modernization of production and housing construction.

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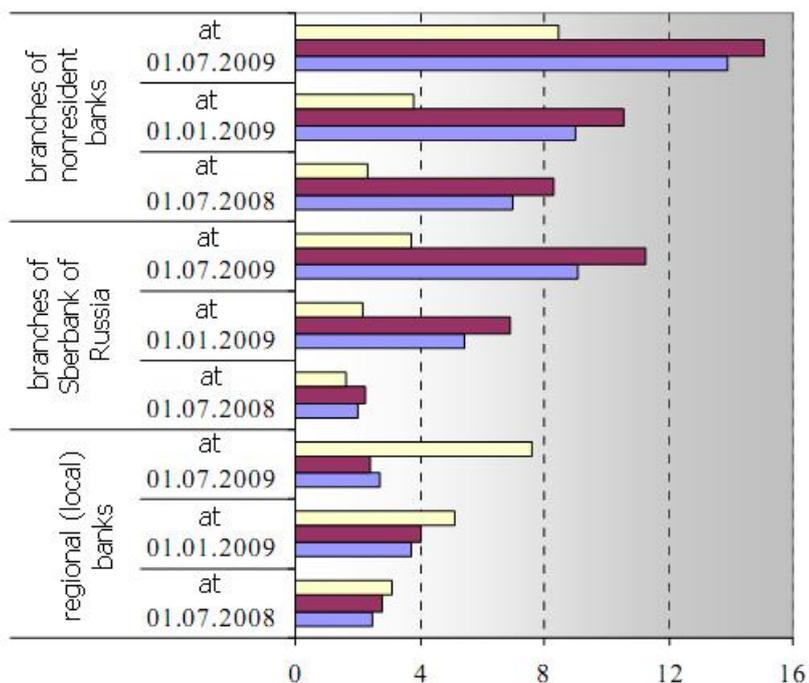
Russia



	2001	2002	2003	2004	2005	2006	2007	2008	2009*
Russia's GDP (% Growth in constant prices)	110,0 %	105,1 %	104,7 %	107,3 %	107,2 %	106,4 %	107,4 %	108,1 %	91,3%
GRP Kaliningrad (% Growth in constant prices)	103,4%	109,5%	109,3%	112,6%	103,6%	111,6%	124,7%	115,9%	86,2%

* Forecast for 2009

Share of overdue credit organizations operating in the Kaliningrad region (% of the total value of debt)



Current economy of Kaliningrad and the situation of energy demand

By Volkmar Wulf

Introduction and current economic situation of Kaliningrad

The present state of impact of the global financial crises reached Kaliningrad a Russian (RF) Exclave within the European Union at the Baltic Sea. The situation of the economy of Kaliningrad became in the first half of the year 2009 apparent more poorly than expected. However the situation differs from branch to branch. Some industry sectors have real problems others are still in relatively good conditions. This might change by the end of 2009 and in 2010 if the devaluation of the Rouble against the EUR raises the cost of goods produced by Kaliningrad's processing companies and reduces the competitiveness on the RF – and / or EU and Global Market. Many companies have reduced their employees or they work only two days or half days a week (but the salary of employees is reduced to their working time). Nevertheless when going through the streets and supermarkets, or look into the restaurants of the city of Kaliningrad or those towns in the vicinity of the region one gets the impression that there exist no crises. But this situation is deceptive as the Kaliningrad economy is quite sensitive to change of scene. However, in the first half of 2009 the index due Kaliningrad Statistical Office of industrial production reached 84,1 % (on the average across the Russian Federation – 85,2 %). On average for June, 2009 the index of industrial production has grown slightly by 32,8 % (across the Russian Federation by – 4,5 %). The volume from processing industry for shipping goods of own manufacture from Kaliningrad reached 74.449 million RUB. The index of processing industry in the time from January till June 2009 reached 74,7 % against 114,5 % in the same period of 2008. It is necessary to note, that in relation to the corresponding months of the year 2008 there was a positive dynamics of growth to be recognised which means that in 2009 one can see a serious recession in production. This has negative consequences to one of the main processing industry sector in Kaliningrad as: of production of electric equipment, electronic and optical equipment. This production line have been reduced due the official index by 55,9 % compared to the level of the year 2008. On the other hand showed the index of manufacturing and distribution of electric power, gas and water in the first half year 2009 only 81,9 % and for June 2009 – 240 % due to repair of the Kaliningrad main power station – TES – 2 which produces approximately 70 % of the electric power for the region. Even in the declining of production in the processing industry and in those time of recession with some slightly growth in the middle of 2009 prices for electric power increases by roughly 25 %. Well, the total building and construction industry went also down and was characterized by a decrease due to the financial and economic crises in the world and which has hid Russia and its Kaliningrad Region at the Baltic Sea, the Russian Exclave within the European Union.

Kaliningrad Region and its Energy Production and Development

a. General and Current Situation

But on the other hand Kaliningrad Region looks and has to look further beyond the financial and economic crises. When economy in Kaliningrad develops in line with the Medium and Long Term Development Strategy the area will be prepared to solve the demand of energy by following sets of points:

- development of the transport infrastructure
- development of the power industry infrastructure
- development of the agro – industrial sector
- development of the tourist and recreation sector

The special geographical position of Kaliningrad at the Baltic Rim defines prospects of development of a fuel and energy complex and an infrastructure as a whole in close interaction with the neighbouring countries. The regional Government sees the following additional main tasks in the area:

- ensuring the power safety of the region and effective social and economic development
- formation of competitive export oriented economy and its integration into the world market

Taking this into account the government of the RF and of the region knows that there is already a huge lack of energy and for meeting this future demand Kaliningrad defines prospects of development of

energy complexes and an infrastructure as a whole and wishes to do this in close interaction with the neighbouring states and so Kaliningrad started a set of special energy actions. The main problem occurs for Kaliningrad Area when the Atomic Power Station Ignalina in Lithuania will be closed by the end of 2009. Lithuania provides Kaliningrad electricity from this Power Station. Another problem concerns the gas and electricity delivery from the RF (i.e. electricity from different Power Station but mainly from the Smolensk Atomic Power Station). This electricity reaches Kaliningrad through Bella Russia, Estonia, Latvia and Lithuania. This long way is a costly distance and loss of energy is pre – programmed. The analysis of current situation in electric power industry of the region shows, that the area has a great deficit of energy. The current energy consumption in Kaliningrad (fig. 2008) area reaches about 4 billion KW/h. Thus the share of export was 30 %. In the long term the energy consumption will increase. The Power Stations in Kaliningrad produce currently only about 2,83 billion KW/h. The different is "import" of energy from neighbour countries or from the RF. Nevertheless the demand of energy in Kaliningrad increases rapidly in future due to the strategy and programme of the Russian government and that of the region for new investments in industry and agricultural industry etc.

b. Kaliningrad and the EU Baltic Energy Ring

Referring to these above views and in this case it will be necessary for Kaliningrad of being a partner of the creation of a *Baltic Energy Ring* as a model for a Common European Energy Space with participation of not just direct neighbours of Kaliningrad but of total Baltic Regions. However, there exists already a network between the Baltic States and from Estonia to Finland and from Lithuania to Sweden. But somehow Kaliningrad Area seems to be excluded. Therefore it will be necessary that this area is linked to a Baltic Energy Ring and the EU Energy Network. In this respect one should not overlook the report from Mrs. Magdalene Hoff MEP and her interview in the Kaliningrad Pravda on July 26th, in the year 2001 when she as the head of the EU – Parliament Delegation in Kaliningrad emphasizing that the European Union will not isolate Kaliningrad. She even referred to the former agreement between the Russian Federation and the European Union, that encourages the process of integration on the regional level and to the Nida Initiative and also the EU Parliament initiative from 2001 and the challenge for Kaliningrad Oblast. Well, an other point is that the Russian – Danish Energy Efficiency Project and the Kaliningrad City Hall, which is a co-operation in energy saving, the Danish energy Agency and the Danish Technological Institute could be the base step to integrate the Kaliningrad Region into Baltic Energy Ring and EU Energy Network.

c. Kaliningrad challenge and problems in climate change and integration of Energy Charter Treaty and energy partnership

Well, Kaliningrad faces a series of challenges too including resources degradation, climate change and other problems. The Kaliningrad Government takes every possibility into account for an integrated energy and climate change policy. This is in line with the conceptual approach of the RF Government to review the Energy Charter Treaty of the signatories from 1990. As it is well known RF's non – ratification as the rejection of the entire process, Russia did not withdraw its signature from that Energy Charter Treaty uses the treaty provisionally accordingly. The President of the RF, D. Medvedev, said in Helsinki in spring 2009 "...global energy cooperation should replace the 1991 Energy Charter Treaty. Actually one should not overlook that the EU's new European Neighbours to the East do not only belong in Europe in a geographic sense, as their citizens also consider themselves European by virtue of common experience and culture, not least because of their Christian roots. However, it must be understandable, that here the RF Exclave in the EU, should be taken into common concern of the EU especially what relates to energy partnership of the Baltic Rim and the EU. A more sustainable longterm development model of the future requires a modern global energy supply system which would be adequate to the current conditions", President Medvedev said. The existing bilateral arrangements and multilateral legally binding norms governing international energy relations have failed to prevent and resolve conflict situations. Therefore it will be necessary to

efficiently improve the legal framework of the world trade in energy resources to avoid further conflicts also for instance at the Baltic Area. To take this into account, that Kaliningrad is somehow excluded from the Baltic Energy Ring the new conflict will be programme in the Baltic Area. The closing of the Igalina power station in Lithuania and occurrence of deficiency of the electric power in Lithuania (up to 500 MWh) will lead to essential restriction of transit of the electric power in the Kaliningrad area from the RF for completion of regional deficiency. The question of maintenance of power safety of the Kaliningrad area and effective social and economic development connects the Government of the area with the end construction of the Kaliningrad TES – 2 (Thermal Power Station – 2), designing other generations of capacities with combined development electric and thermal energy in the cities. Kaliningrad having developed systems of the centralized heat supply, development of renewable energy sources, effective Energosperejnenii. The current TES – 2 Block produce only about 67 % of energy for the Kaliningrad Area. However, on June 6th, 2009 it was agreed with the RF Minister of Energy and Power, Mr. S. I. Shmatko, to establish a new second TES 2 Block for another 450 MW. The target is to bring this block on the electric power network in November 2010 for the Kaliningrad area.

d. Renewable Sources for Energy and the Baltic State Interconnection Energy

Well, as mentioned above by President D. Medvedev in spring 2009 and also in line with the views of the Minister of Energy and Power of Kaliningrad the regional Government recognizes that the region should develop a programme of renewable energy sources. In this respect one of the mechanisms of attraction of means for realization of action of the programme will be state – private partnership. The purpose and problem of the state in the field of use of renewed sources are:

- the basic parameters of development of electric power industry with use of renewable energy sources
- list of measures of provisions of economic incentives and support of development of electric power industry on the basis of renewable energy sources
- list of organizational measures of support of development of electric power industry on the basis of renewed energy sources
- target parameter of volume of manufacture of electric energy with use of renewed energy sources for the period till 2020 and beyond. In 2020 renewable energy share should reach more than 4,5 of the total energy consumption of Kaliningrad.

This basic programme could be also one of the parts of the energy and eco – efficient economy provided by Kaliningrad and governing the climate change within Baltic Region States Interconnection Energy Plan.

For Kaliningrad region this new Baltic State Interconnection Energy (see also point b above) Plan is isolating Kaliningrad completely when the action plan of the eight Baltic States signed on June 17th, 2009 together with Denmark, Germany, Poland, Finland and Sweden will come into force. This plan and strategy is to connect Lithuania, Latvia, and Estonia with the EU Energy Network. Part of the action plan is to implement a number of energy infrastructure and market restructuring projects identified in the Baltic Energy Market for a more integrated electricity market in the Baltic Region in accordance with the European Commission's Second Energy Review from November 2008. The target of the plan is to extend the liberalisation of the Nordic Electricity Market. It might be that currently a problem could be the removing of regulated tariffs and cross – border restrictions etc. for the Kaliningrad region as a Russian Exclave within the EU. However, this could be solved in negotiation with the Russian Government so that Kaliningrad could be part and to be connected and integrated into this European plan and finally to the European Electric Network.

e. Existing Electric Power Station and Future Energy Power possibilities

However, one should not lose the sight, that the existing electric power stations in Kaliningrad are very old excluding TES – 2. There are for instance one in Svetley close to Kaliningrad City and one in Gusev not so far from the Lithuanian border. For instance the power station in Gusev was established in 1934 in the German time and has been taken into operation in 1935 for producing electricity. After the end of the war in 1945 this station has been rebuild but what was usable from the previous time, has been integrated into the

construction. 1947 the power station has been nearly ready for producing electricity but it took some more years and at least in March 1955 the first electric power has been produced. End of 1950s the power station has been changed to heavy oil (Masut). The power station currently produces electricity and heat for the city of Gusev and the region. However, the heat power for the city and the area is stopped yearly from April 15th till October 15th. In future the power station will be changed from Masut to Gas, which is delivered from the Gas regions in the Russian Federation. But this does not change the age of the power station.

As mentioned several times above TES – 2 life Power Station of Western Russia is the important and modern facility in Kaliningrad region. TES – 2 is the most modern plant with two modern SIEMENS turbines. The power station with its first Block was established in October 2005. The equipment used here is in a sense unique. It was mainly manufactured in the RF (including the SIEMENS turbine under license). The capacity of the TEC – 2 first Block unit reaches by full power 450 MW. The total capacity of the power plant will reach 900 MW after the second Block will be ready in November 2010. The technology based on the steam and gas cycle will enable to increase the efficiency to 51 % (at ordinary power plants with steam power aggregates the efficiency does not exceed in the Kaliningrad area 40 %), to save up to 20 – 25 % of fuel and reduce pollution air emissions by 1/3. After the second Block of TES – 2 will come into operation the electricity production in the region to develop large scale industrial production with many new workplaces, thus creating a resource basis for attracting investment in Kaliningrad as mentioned above.

f. Renewable Energy Development and Problems

Well, some points mentioned above of the strategies for development of electric power industry mentioned above by President D. Medvedev concern the part of renewables but not mentioning those in detail as for instance Bio Fuels and Bio Gas, Wind Energy, Cogeneration = Combined Heat and Power Generation, and Energy Recovery from Waste by Waste Incineration or electric power station by watercraft. As in the next few years in Kaliningrad five new, but small, electric and heat power stations for the narrow and close regions will be established. The base possibilities for the different power stations are given. As far as information are provided by authorities the various possibilities are discussed in working groups examine which sector of the power station based on renewable "material" will provide the best and efficient power for the region.

Concerning Wind Energy, the established capacity of Wind Energy in Kaliningrad produce about 5,1 MWh and in total RF 14,1 MWh. The total energy in the Kaliningrad territory of Kaliningrad is estimated by 1100 MWh. The use of Wind Energy Stations / Parks can only be recommended in the coastal zone of wind activity. However there are plans that prospects of development of wind parks in water areas of Lithuania, Poland and Kaliningrad area at the coasts of the Baltic Sea particular in water area. Yantarengo of Kaliningrad plans a project of a Wind Energy Park with 50 MWh in the Baltic Gulf. That park could perhaps cover 25 % of electric power consumption in Kaliningrad. But one has to take into consideration that Kaliningrad Region and the neighbouring countries are part of the bird migration route. Wind energy parks could disturb the bird route in spring and in autumn.

Well, an ambitious renewable energy policy in Kaliningrad is not yet completely seen. Lots of work has to be done. One sector is the clear directive of legislative law and regulation energy power and industry interests on energy out of renewable material. One could be the "copy" of the EU recycling strategy. That strategy is targeting on prevention and recycling waste to pave the way towards a recycling society by decoupling economic growth from resource use. As the living standard in economy rises after the current crises natural resources even in the RF and so especially in Kaliningrad will not be available for use for ever. However, renewable on the other hand could spearhead regional market integration in Kaliningrad together with its Baltic Neighbours, if the Baltic States together take the advantage of the cooperation mechanisms in this area. A binding target to satisfy the energy consumption from renewable energy for instance from waste in the frame of cogeneration is very challenging for the electricity industry, which will have to produce perhaps 35 % of total electricity from renewables. Cogeneration (CHP) would bring Kaliningrad closer to its energy related goals. It is a proven tool to increase energy efficiency and to achieve energy savings' targets. It contributes a high percentage of annual primary energy savings objectives. It reinforces efforts to fight climate change by reducing

CO2 emissions and decreasing electricity network losses. The technology for cogeneration is on the market for decades, the common perception is that cogeneration is in the opinion of the engineers of administration archaic, particular when compared to new technologies, such as solar panels or Nuclear Power Stations as planned in Kaliningrad close to the Lithuanian border. Moreover, the use of fossil fuels for instance in cogeneration is considered unattractive, and knowledge of the efficiency and potential uses of biomass or waste for energy recovery etc. is not widespread. One should keep in mind that especially in Kaliningrad and might be in other RF areas too, waste is mainly land filled in deposits but also thrown into the landscape. (See *ECAT STUDY – Environmental Situation in Kaliningrad from 1999*) Landfill not only takes up more and more and more valuable land space, it causes air, water and soil pollution, discharging carbon dioxide (CO2) and methane (CH4) into the atmosphere and chemicals and pesticides into the earth and groundwater. This in turn is harmful to human health, as well as to plants and animals. In waste we have the best recourse for Cogeneration. It depends for small demand one can establish a small cogeneration plant or if necessary a large cogeneration station for heat and electricity. Large CHP facilities have in general lower production costs than small units. Kaliningrad region at the Baltic Rim is a small area and avoiding cost from long distance transport of energy from the Russian main territory cogeneration could be one sector for energy demand in future by incineration of waste in combination with bio gas or bio fuel. By selecting waste for incineration useable raw material will be separated for recycling and also other important resources will be protected for other important purpose.

g. Nuclear Power Station

Last intention for energy development is the plan of Kaliningrad and the Russian Government to establish a Nuclear Power Station in Kaliningrad Region close to the Lithuania border. This power station has among experts no unanimity as to how realistic; environmentally sound of economically viable are the plans to create a nuclear power station together with a French Company. On the other hand Iglanina in Lithuania will be closed under the pressure of the European Union and not far away from that power station a new nuclear power station will be established. The Kaliningrad regional authorities at the moment are strongly in favour of that plan and some practical steps are made already in the direction of that plan. The Government of Kaliningrad Region and investors as well of the construction bureau have signed a contract for that Baltic Atomic Power Station. Well, in addition, the Russian Ambassador for Lithuania, Dr. Vladimir Tschchikvadse, in August this year required that Lithuanian investors should or could participate in the creation of the nuclear power station "Baltijskaja". The demand, he said, reaches about six billion EUR (€) by private investors. It is possible, that foreign investors participate but the main shares will be kept in the hands of the Russian Federation. The Russian Federation argues that it is cheaper for Lithuania to participate at the Russian Power Station than to reconstruct an own one. However, Lithuania prefers as mentioned above to establish together with Poland, Sweden, Latvia, Estonia and the other States of the Baltic Sea Area a common EU Energy Ring. The Kaliningrad Atomic Power Station will provide the Kaliningrad Area with electric power especially for use in industrial industry. The station will be build by Russian companies which are part of the holding "Atomenergoprom" in St. Petersburg. It is estimated that the Nuclear Power Station of Kaliningrad will after termination in 2016 or 2018 manufacture electricity by two power units 2.300 MWt. And later there will be the possibility to export electric power of 900 and 1.700 Mwt. to the neighbourhood countries. On June 6th, this year a conference took place in

Kaliningrad with the Russian Minister Sergey Shamtko and nearly all general directors (CEO) of the largest generating and electricity network power station in the Russian Federation. The key issue was the construction of the Nuclear Power Station in the Kaliningrad Region as well as:

- necessary changes to be introduced into legislation taking into account the peculiarities of the Kaliningrad Region situation;
- development of the electricity grid and of the infrastructure of the region with regard to the planned commissioning of new generating capacities;
- Prospects of electrical power import / export organisation, ensuring the full – capacity operation of TES – 2 power Station;
- and finally how shall the radioactive nuclear waste be handled. This important item should be solved before the power station is been build. There are many doubts that it is possible to transport that special waste through Lithuania and Bella Russia or by ship via the Baltic Sea or to keep these waste it in the permanent disposal in the Kaliningrad Region. And on the other hand, nuclear energy is one of the cleanest if handled the condition which is necessary so that no harm will occur for the public.

Energy of all kinds including nuclear energy is on the other hand important to be developed in total because it is necessary in the Kaliningrad Region for the future to guarantee the prosperity and economic situation of the Kaliningrad Region in future and make the region attractive for the people / inhabitants and investors.

Conclusions

The problem for Kaliningrad is although, practically and finally currently the complete absence in the RF of legislative initiatives on development of the market of the renewed energy sources operating in many industrialist countries of the world. Further the laws and regulations as well as the stimulation of the inhabitants are missing. However, it should not be denied that first signs are there in Kaliningrad in this respect. Some schools do teach or instruct pupils about environment etc. and to help collecting waste (perhaps once a year) from landscapes as beaches, forest or environment of housings and living places. But this waste will be collected and thrown into bins and transported to the landfill, which is not the renewable view of the Russian President D. Medvedev or Prime Minister V. Putin. Well, it is necessary, that the Kaliningrad area will be the first region in Kaliningrad taking care of the transformation planed of Prime Minister Putin to change the economy in Kaliningrad away from the raw material delivery towards a real industry and processing industry sector with a large small and medium size companies and job – sharing sectors. Naturally the European Union has to play its strong card too and is responsible for that what has been said in the past: the European Union will not isolate the Kaliningrad Region. Russia and here Kaliningrad is the key to the Baltic Sea Region.

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