PUBLISHED BY
VOPROSY
EKONOMIKI
N.P.

Available online at www.sciencedirect.com

ScienceDirect

Russian Journal of Economics 3 (2017) 54–70

Russian
Journal of
Economics

www.rujec.org

Eurasian Economic Union: Current state and preliminary results ☆

Evgeny Vinokurov

Center for Integration Studies, Eurasian Development Bank, St. Petersburg, Russia

Abstract

This paper assesses the current results of the establishment of the Eurasian Economic Union (EAEU). On the one hand, the EAEU has not been an impeccable "success story". The EAEU's progress has slowed after initial rapid progress. On the other hand, it has achieved much. The EAEU is best viewed not as an exception to general rules of regional economic integration, but rather as a functioning customs union with its own successes and stumbling blocks, enriched by several additional quite developed areas of economic integration. This paper reviews the state of Eurasian institutions, the single market for goods and services, the state of mutual trade and investment flows among member states, ongoing work to eliminate non-tariff barriers, problems pertaining to the efficient coordination of macroeconomic policies, progress toward establishing an EAEU network of free trade areas, the state of the common labor market, and the dynamics of public opinion relative to Eurasian integration in the five member states.

JEL classification: F13, F15, F36, F45, F53, G38.
Keywords: Eurasian Economic Union, regional integration, customs union, common market, non-tariff barriers, free trade area, foreign direct investments.

1. Introduction

The Eurasian Economic Union (EAEU) is a newcomer among regional integration organizations. It has been operating as a customs union since 2011, and as an economic union since 2015. In addition to geopolitical objectives, it is

☆ The updated English version of the article published in Russian in *Voprosy Ekonomiki*, 2016, No. 12, pp. 43–60. A shorter earlier version of this paper has been published in German in *Osteuropa*, 2016, No. 5, pp. 129–140 under the title "Unter Partnern. Ein nüchterner Blick auf die Eurasische Wirtschaftsunion."

E-mail address: vinokurov_ey@eabr.org

Peer review under responsibility of Voprosy Ekonomiki.

http://dx.doi.org/10.1016/j.ruje.2017.02.004

based on a specific long-term economic agenda. In this context, the EAEU was established to help its member states make the most of intraregional economic ties, modernize their national economies, and forge an environment conducive to improving their global competitiveness. A single market for goods, services, capital, and labor is at the heart of the Eurasian integration process. The EAEU has already been reinforced with supplementary integration infrastructure, including the EAEU Court, the Eurasian Development Bank, and the Eurasian Fund for Stabilization and Development.

Establishing the EAEU was a major achievement for its members after they had repeatedly endured two integration “false starts” in the 1990s and 2000s (namely, the 1995 Customs Union and the 2003 Common Economic Space idea; see below), but they still have many obstacles to clear.

The Union is already a functioning entity. This statement does not raise any particular objections, unless the bar is set too high, and when compared to the European Union, the regional integration benchmark, expectations are set too high. However, if the bar is set lower, with the EAEU placed alongside other regional integration projects with varying levels of depth and success — NAFTA, MERCOSUR, ASEAN, Cooperation Council for the Arab States of the Gulf (GCC), South African Customs Union (SACU) — then a more adequate framework for analyzing the relative standing of the EAEU becomes feasible.

We maintain that the EAEU is best viewed not as an exception to the general rules, but rather as a functioning regional integration bloc with its own successes and problems. The Eurasian Union has major achievements, but it also has deeply embedded limitations. By 2016, the initial momentum had petered out, as we will show in our subsequent analysis. Now the integration bloc is entering its first wave of conflicts and challenges. Will it be able to continue its development? Or will it regress?

Our objective in this paper is actually quite modest. It aims to provide the reader with a very condensed descriptive analysis of the EAEU, covering as much data as possible. We think that such a “little primer” is sorely missed in the literature.

We will address the following topics. First, we will take a brief look at the current state of Eurasian institutions (not just the EAEU, but the entire Eurasian economic integration ecosystem) and their evolution. Second, we will consider the emergence of common markets for goods and services and the status of trade and investment flows between EAEU member states. Third, we will examine the progress towards eliminating and unifying non-tariff barriers. This work may have a very substantial effect, far exceeding the impact of eliminating tariff restrictions. Fourth, we will look at the behavior and structure of trade flows. Fifth, we will review the flows of mutual investments within the EAEU. Sixth, we will explore the content of the EAEU Treaty and the issues related to its implementation, particularly as they relate to the coordination of macroeconomic policies, including monetary matters. Seventh, we will analyze the ongoing efforts to set up free trade areas and sign trade and economic cooperation agreements, including those with two key trade and investment partners — the EU and China. Eighth, we will examine the common labor market already in operation. Finally, we will consider the changing public perception of Eurasian integration.

2. Evolution of Eurasian institutions: From two false starts to a functioning customs union

From an ideological perspective, this large-scale international project was born in a speech given by Nursultan Nazarbayev, President of the Republic of Kazakhstan, in March 1994 at Moscow State University. President Nazarbayev's speech presented a trailblazing integration paradigm emphasizing the need to create an Eurasian Union with a clear focus on economic matters. In practical terms, the starting point was the year 2007 (see below).

It has taken 20 years to implement the integration idea, and there were several false starts along the way. During that time, the Commonwealth of Independent States defused many serious threats of disintegration. The Transport and Electric Power Industry Councils, which managed to ensure technological cohesion and preserve power systems, have played a special role. Still, for a number of objective reasons, as an organization, the CIS has only managed to secure a "civilized divorce".

In 1995, the "Troika" (Belarus, Kazakhstan and Russia) — the three countries that still form the nucleus of the integration association (Vinokurov, 2010) — signed the Customs Union Treaty. That instrument was designed to remove barriers hampering free economic interactions between economic agents, facilitate free exchange of goods, and assure good-faith competition between the parties. This was false start No. 1.

In 2000, five states established the Eurasian Economic Community (EurAsEC). More than 100 agreements were signed under the aegis of that entity. Moreover, the EurAsEC was to become an institutional springboard for initiatives that would materialize in 2006–2010. Thus, the Customs Union Commission was technically a EurAsEC body. EurAsEC was officially dissolved on January 1, 2015, concurrently with the establishment of the Eurasian Economic Union.

In 2003, the presidents of Belarus, Kazakhstan, Russia, and Ukraine signed an agreement to create a "Single Economic Space". The Orange Revolution of 2004 put an end to that undertaking. This constituted false start No. 2.

In October 2007, the presidents of Russia, Belarus, and Kazakhstan signed the Agreement on the establishment of the customs union (CU). They also approved a two-year implementation plan. The objective was to facilitate free movement of goods in mutual trade, create favorable conditions for trading with third countries, and expand economic integration.

Quite a few people subscribed to the idea that the third attempt would also result in a failure. However, upon expiry of the scheduled two-year preparation period, on December 19, 2009, Alexander Lukashenko, Dmitry Medvedev, and Nursultan Nazarbayev met in Almaty to sign the Joint Statement on the Establishment of the Customs Union. Consequently, the Common Customs Tariff went into force in 2010. This success was at least partly attributable to the economic crisis, which encouraged the three countries to accelerate their integration efforts.[1]

[1] The standard theoretical argument is that crises discourage integration because they foster protectionism. There is also a different line of reasoning that applies to the Former Soviet Union: economic crises may catalyze integration if the countries involved are closely connected and have no viable alternatives (Vinokurov and Libman, 2014).

In 2011, the CU was already working at full capacity, with economic agents operating within a common customs territory and using the Common Customs Tariff. On January 1, 2012, the CU was supplemented by a package of further seventeen agreements that constitute the regulatory basis for the Single Economic Space (SES). Those agreements address a number of key issues underpinning the process of economic convergence within the "Troika", ranging from coordination of macroeconomic policies to labor migration.[2]

Finally, on January 1, 2015, the Eurasian Economic Union Treaty came into effect. Armenia acceded to the integration association on January 2, 2015, and Kyrgyzstan on May 8, 2015 (the decision was ratified and took effect in August 2015).[3]

3. EAEU institutions

The "family" of EAEU institutions is now complete. The Supreme Eurasian Economic Council, a body made up of the heads of member states, addresses critical matters affecting the Union and approves its strategy, key operating areas, and development prospects. The Eurasian Intergovernmental Council, which comprises the heads of the governments of the member states, exercises its powers in 10 areas, including enforcement and oversight of the EAEU Treaty and approval of a draft EAEU budget.[4]

Since 2012, there has also been a common supranational institution acting as the Union's regulatory body and a motive force for integration — the Eurasian Economic Commission (EEC). Approximately 140 competencies have been elevated to the Commission's supranational level. The EEC's main executive body is the Board, comprising 10 members (ministers), with each member state represented by 2 such ministers. Such a representation scheme diminishes Russia's role as the region's leading state in Eurasian Economic Union affairs: despite being responsible for 87% of the Union's total GDP, Russia has only 20% of its total voting power. This was intentional. Since February 2016, the Commission has been headed by Tigran Sarkisyan, former Prime Minister of Armenia.

Other key EAEU bodies include the following:

The Court of the Eurasian Economic Union is a specialized judicial body authorized to resolve disputes related to the implementation of international treaties concluded within the framework of the Union, and enforcement of the decisions of its governing bodies. Its rulings, for example, decisions on the Common Customs Tariff, have direct effect in the EAEU's countries and are legally binding. As of today, the Court has primarily reviewed claims concerning setting the particular import quotas of the Union.

Financial mechanisms of Eurasian integration are realized within the framework of the Eurasian Development Bank (EDB) and the Eurasian Stabilization and Development Fund (ESDF). The EDB (6 member states, paid-in capital of $1.5 billion, current investment portfolio ca. $2.2 billion) is a functioning regional international financial institution. Over 10 years, it cumulatively invest-

[2] More analysis on the Single Economic Space can be found in Dragneva and Wolczuk (2013).

[3] Detailed surveys of the evolution of Eurasian integration can be found in: Hancock and Libman (2016), Dutkiewicz and Sakwa (2014), and Libman and Vinokurov (2012).

[4] The EAEU's core legal document is the Eurasian Economic Union Treaty (see http://www.un.org/en/ga/sixth/70/docs/treaty_on_eeu.pdf).

Table 1
EAEU socioeconomic development indicators, 2015.

Indicator	Armenia	Belarus	Kazakhstan	Kyrgyzstan	Russia
GDP					
Nominal, $ billion	10.5	55.0	184.4	6.5	1 331.1
Purchasing power parity, $ billion	23.1	164.3	399.6	18.5	3 402.9
Nominal per capita, $	3 515.0	5 754.5	10 508.3	1 112.8	9 054.9
Population, million people	3.0	9.5	17.7	6.0	146.5
Foreign trade, $ billion	4.7	57.0	75.9	5.7	526.3

Sources: IMF; World Bank; national statistic agencies; author's calculations.

ed ca. $4.85 billion, while prioritizing projects promoting mutual trade and mutual investments (EDB, 2016). The ESDF, with capital of $8.5 billion and the same six member states (all five Eurasian Union members plus Tajikistan), is a key player in regional crisis management and financial stabilization. Essentially, the ESDF is a "regional IMF", acting primarily as the lender of last resort in extending public budget loans. It also specializes in preferential lending to finance infrastructural projects.

The bottom line is that a regional integration association has been created with a common market of 182 million people and an aggregate GDP of approximately $2 trillion. The Union's largest economies are those of Russia and Kazakhstan (Table 1).

4. Elimination of exemptions in the single market for goods and services

The progress of Eurasian integration depends on the success of "bottom-up integration"—growth of mutual trade, mutual investments, and civilized labor migration. This requires that the "rules of the game" be uniform within the EAEU economy. The ultimate goal in the long term (until 2025) must be to increase the common market as much as possible.

The events of 2015–2016 suggest that this is a tall order.

Elimination of exemptions in the single market is critical to the modernization and cooperation of EAEU economies. For example, the parties have agreed to create, as of January 1, 2016, a common market for pharmaceuticals and medicines. However, due to regulatory complexities and difficulties associated with unifying the procedures governing pharmaceutical operations through the entire EAEU, the corresponding decision has been delayed by one year. Moreover, in order to make the decision politically acceptable to all member states, the fundamental move to the truly common market has been postponed to 2020 and in some parts even to 2025.

Additionally, negotiations regarding the EAEU Customs Code have been anything but easy. The code should have gone into effect on January 1, 2016, but its adoption was delayed. Member states' economic agents are now operating without the code, relying on national laws and existing treaties and agreements. The EEC has received approximately 1,500 comments on the draft code from Belarus, Kazakhstan, and Russia. Armenia and Kyrgyzstan joined the work on the document later than the other EAEU members and are now also engaged in an active discussion of proposed amendments. In June 2016, 57 matters related to customs regulation within the EAEU remained unresolved. A discussion at the level of prime ministers of five states (Intergovernmental Council, November 16, 2016) was necessary to finally remove the last obstacles. The EAEU Customs Code will thus come into effect by mid-2017.

There are several other sensitive issues that continue to foment discord.

One such issue is the unwillingness of EAEU countries other than Russia to adopt the sanctions that Russia has imposed on Ukraine. Those countries continue to conduct business with Ukrainian companies. Russia never issued official recommendations to adopt the sanctions, nor was the issue escalated to the level of the EEC. Meanwhile, a conflict of interests has arisen (in substance, if not in legal terms) between Russia's foreign policy and its trade relations with other EAEU countries.

A second issue is Belarusian manufacturers' and trade companies' re-exportation of EU goods, which are subject to Russian counter-sanctions (mostly, food products). For example, "Belarusian" bananas and oysters have been shipped to the Russian market. Accordingly, Russian authorities began inspecting all incoming cargo to verify that the goods came from their stated countries of origin. That resulted in considerable delays, queues at the Belarusian–Russian border, and complaints from Belarusian authorities. Eventually, the issue was resolved by imposing more stringent country-of-origin labeling requirements and introducing harsher penalties for Belarusian exporters' non-compliance.

Relations between Russia and Ukraine deteriorated even further in 2016 when Ukrainian activists began blocking Russian vehicles moving through Ukrainian territory. In response, Russia imposed similar counter-measures on Ukrainian vehicles. That significantly handicapped Ukrainian exporters trying to deliver goods to Kazakhstan via Russia (though Russia may likely have been the true final destination for a significant portion of cargo supposedly going to Kazakhstan). A partial solution was offered by the EAEU Cargo Transportation Information System, and Ukrainian carriers eventually received the ability to make transit deliveries through Russian territory.

By the same token, there has been some progress in eliminating the exemptions stipulated by the EAEU Treaty. Preparations are underway to establish a single power market. A corresponding international treaty will be prepared after the EEC has approved the conceptual framework for the single power market. According to the current schedule, the market will be launched in 2019. The details are still under discussion. The barebones option is a common spot market combined with cross-border power exchange mechanisms (it could be codenamed "Nord Pool Minus" referring to the Scandinavian common electric power market).

EAEU member states are beginning consultations on a very complex matter—creation of an EAEU financial regulator by 2022–2025, a supranational financial institution that would be responsible for enforcing common standards in the Union's financial markets and for providing proper regulation and supervision. No issues related to a single central bank or single currency have been officially raised to date.

A single market for oil, gas, and petroleum products is expected to emerge by 2025. The distant deadline is due to the oil and gas sector's extraordinarily important role as the source of national budget revenues. The work will proceed separately (for oil and gas) under two programs and according to two roadmaps.

The efforts related to the finalization of the Customs Code and the creation of common pharmaceutical, power, oil, and gas markets and a single financial regulator represent components of the same process — elimination of exemptions from the EAEU Common Market. In practical terms, that process is rather convoluted and controversial. It is only logical to assume that the final solutions will be the product of mutual concessions.

5. Elimination and unification of non-tariff barriers

One of the most important matters on the EAEU agenda in the immediate future is the gradual unification and elimination of non-tariff barriers (NTBs) in mutual trade in goods and services. Non-tariff barriers place a significant burden on mutual flows of goods and services between EAEU countries, reducing the overall efficiency of the common market. They have a particularly pronounced crippling effect on the development and cooperation of hi-tech industries, particularly mechanical and chemical engineering.

The EDB Center for Integration Studies completed a large-scale research project and, for the first time, gave an extended assessment of the impact that NTBs have on mutual trade within the EAEU and developed recommendations on how to eliminate such barriers. A massive survey involving enterprises from Belarus, Kazakhstan, and Russia found that NTBs account for 15% to 30% of total export value. In other words, each dollar's worth of export goods traded between EAEU countries still includes 15 to 30 cents of NTB-related costs as of 2014 (Vinokurov et al., 2015).

NTBs can be conveniently divided into two groups. The first group includes such non-tariff barriers as sanitary and phytosanitary measures, technical barriers to trade, quotas, bans, and quantitative control measures. The second group comprises price control measures and measures that affect competition (special importers, restrictions on marketing and public procurement, subsidies). Barriers in the second group are often described as "sand in the wheels", as they hinder the movement of goods and, in theory, can be completely eliminated. These non-tariff barriers have the most negative impact on trade.

In the medium term, Belarus will benefit the most from the reduction of NTBs: its real GDP may increase by 2.8%, and its wealth could rise by 7.3% on a cumulative basis. In Kazakhstan, wealth would rise by 1.3%, while real GDP may increase by 0.7%. The effects on Russia may be less impressive: wealth would rise by 0.5% on a cumulative basis, while real GDP would rise by 0.2%. This is attributable both to the large size of the Russian economy and to the fact that Russia relies on trade within the EAEU less than it does on trade with the rest of the world. The largest beneficiaries of NTB reduction will be manufacturers of machines and equipment. This can be explained by the fact that NTB-related costs in that sector are the highest (Vinokurov et al., 2015).

6. Trends in Mutual Trade within the EAEU

Changes in the value of EAEU member states' exports generally reflect the deteriorating economic situation of the past several years, particularly the sharp decline in hydrocarbon prices. In addition to that, the countries' foreign trade

Table 2
Mutual trade between EAEU member states ($ million).

	2011	2012	2013	2014	2015
EAEU, total					
Exports	63 100.9	68 582.2	64 520.0	57 448.3	45 379.8
Belarus					
Turnover	40 798.6	44 750.5	40 697.1	38 804.5	28 209.0
Balance	–10 432.8	–10 570.5	–5 280.3	–6 356.7	–6 212.8
Kazakhstan					
Turnover	23 029.3	24 626.3	24 603.7	19 665.2	15 780.2
Balance	–8 822.7	–10 950.7	–12 736.5	–9 250.6	–6 006.6
Russia					
Turnover	62 322.4	67 686.0	63 591.3	56 541.5	42 801.2
Balance	19 307.0	21 622.8	18 164.7	15 492.7	14 636.0

Source: Eurasian Economic Commission.

was adversely affected by financial markets' instability ("the parade of devaluations") in 2014–2015. The largest drop of mutual trade indicators was posted in 2015, when total EAEU exports amounted to $45.4 billion, or merely 74.2% of the 2014 level (Table 2) in USD terms.

Despite the decrease in the value of mutual trade, there has been a qualitative improvement in the structure of foreign trade within the EAEU. For example, mutual trade between EAEU member states as a percentage of their total foreign trade has increased from 12.3% in 2014 to 13.5% in 2015.[5] We also note changes in trade balances within the EAEU. For example, Belarus' trade deficit in its mutual trade with the EAEU has declined from $10.4 billion in 2011 to $6.2 billion in 2015, and the trend appears to be sustainable. However, sometimes strong short-term movements do occur. Thus, the Russian ruble's devaluation in 2014 caused a "mirroring" of the structure of mutual trade between Russia and Kazakhstan, and temporarily reinforced Kazakhstan's status as a raw-materials supplier in the EAEU (Alpysbayeva et al., 2015). This situation persisted for approximately one year until Kazakhstan put its currency under a floating exchange rate regime (with a small time lag).

Statistical data on mutual trade exports as a percentage of total EAEU exports also reveal specific patterns (Table 3). During the first year of the EAEU's existence, this indicator increased from 9.5% in 2014 to 10.8% in 2015. In other words, export value in mutual trade among EAEU member states declined less significantly than their aggregate export value.

EAEU imports follow largely the same pattern. Mutual trade imports as a percentage of total EAEU imports amounted to 18% in 2015 *vis-à-vis* 15.8% in 2014 (Table 4). This trend again indicates the growing importance of mutual trade within the EAEU.

In structural terms, mineral products account for the largest chunk of total mutual trade within the EAEU in value terms (33.4% in 2015). However, the second largest product group in total mutual trade is represented by machines, equipment, and vehicles (16.4% in 2015). Agricultural products and agricultural raw materials account for 15.5% of total mutual trade. Therefore, the structure

[5] Here and below, EAEU mutual and foreign trade statistics are based on data published by the Eurasian Economic Commission.

Table 3
Mutual trade exports as a percentage of total EAEU exports (%).

	2010	2011	2012	2013	2014	2015
EAEU, total	9.7	9.8	10.3	9.9	9.5	10.8
Belarus	42.2	36.7	37.2	47.6	44.5	41.2
Kazakhstan	10.0	8.4	7.2	7.0	8.1	10.7
Russia	7.7	7.9	8.4	7.7	7.2	8.4

Sources: Eurasian Economic Commission; author's calculations.

Table 4
Mutual trade imports as a percentage of total EAEU imports (%).

	2010	2011	2012	2013	2014	2015
EAEU, total	15.9	16.2	16.6	15.7	15.8	18.0
Belarus	53.5	56.0	59.6	53.4	55.0	56.8
Kazakhstan	41.4	43.2	38.1	38.3	35.3	36.1
Russia	6.8	7.0	7.1	7.1	7.5	7.7

Sources: Eurasian Economic Commission; author's calculations.

of mutual trade between EAEU member states is qualitatively different from the structure of their foreign trade due to the predominance of products other than raw materials. For example, mineral product exports as a percentage of total exports to third countries at the end of 2015 exceeded 65%, while in mutual trade within the EAEU that indicator was merely 33.4%. At the same time, food and machinery exports as a percentage of total exports to third countries in 2015 was only 7.5%, while as a percentage of mutual trade within the EAEU, these exports accounted for a hefty 32%.

7. Mutual investments: EAEU as a shock absorber?

Adverse economic conditions could not have failed to affect the absolute volume of mutual FDI stock (with 2012 being the peak year). According to data obtained while monitoring mutual investments in CIS countries, EAEU mutual foreign direct investment (FDI) stock as of the end of 2015 stood at $23.6 billion, a year-on-year decrease of 7% (in 2014, that indicator had gone up by 1%) (EDB, 2015; Kuznetsov, 2014). The reduction of the EAEU's mutual FDI stock was due to a decrease of direct investments made by Russian companies in Kazakhstan and Belarus. The main reason for this trend is not completion of investment projects, but rather revaluation of assets following the massive devaluation of national currencies in Kazakhstan and Russia in 2015. However, if we compare mutual FDIs in CIS countries, the situation appears to be much more deplorable. The volume of mutual FDI stock in the CIS has been in decline since 2013. The most notable drop was posted in 2014, when mutual investments in the CIS plummeted by 16% year-on-year, sinking by another 5% by the end of 2015. On the whole, despite the overall instability of the global economy and capital flight from emerging markets, Eurasian Union member states maintain a relatively stable level of investment interaction (Fig. 1).

Predictably, Russian companies with a more than 80% share of exported FDI stock are the largest capital exporters within the EAEU (Table 5).

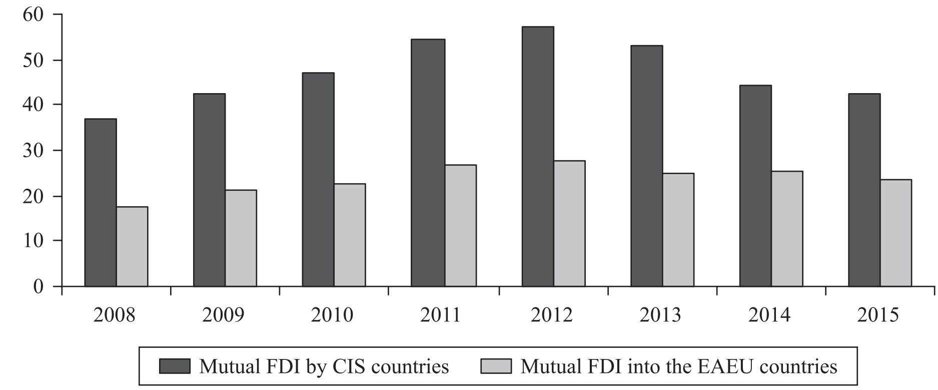

Fig. 1. Movement of mutual FDI stock in CIS countries and EAEU member states ($ billion).
Source: EDB.

Table 5
Mutual direct investments of Russia, Kazakhstan, Belarus, Armenia, and Kyrgyzstan in late 2015.

Recipient country	Investor countries FDI stock, $ million					
	Russia	Kazakhstan	Belarus	Armenia	Kyrgyzstan	Total for the 5 countries
Russia	X	3367	204	3	0	3 574
Kazakhstan	7 095	X	34	0	0	7 129
Belarus	8 297	53	X	10	4	8 364
Armenia	3 056	8	0	X	0	3 064
Kyrgyzstan	811	695	0	0	X	1 506
Total for the 5 countries	19 259	4123	238	13	4	23 637

Note: In line with the methodology used in monitoring mutual investments in CIS countries, only projects with FDI stock in excess of $3 million are included in the database.
Source: EDB.

On the whole, the sectoral structure of FDI in the EAEU is rather diversified, dominated by Russia's traditional industries of specialization. Russian capital investments are dominated by the oil and gas industry (approximately 47% of total Russian FDI in EAEU countries), non-ferrous metallurgy (approximately 18%), and telecommunications (11%). A notable role is also played by the financial and transportation sectors. EAEU countries probably offer Russian investors the most comfortable conditions for foreign operations. The deepening institutional integration is a critical positive factor, in addition to a common historical and economic past, territorial proximity, and linguistic affinity, which ensure a high level of awareness of business customs in the various countries. Kazakhstan and Belarus are preferred investment destinations for many Russian companies, which—at least for the time being—stop short of expanding beyond this range in most production areas, including those with high added value.

In the coming years, the structure of investment flows in the EAEU region will undergo a significant transformation. That transformation will be driven, first and foremost, by the Ukraine's instability, causing the share of EAEU investments in its economy to decline, and by the active expansion of reciprocal ties within the EAEU. The deepening of integration within the Eurasian Union and the emergence of its single market open up new possibilities for corporate interaction, making it possible for "second-wave" investors — which represent a wide gamut of economic sectors — to intensify the formation of cross-border value creation chains.

Therefore, to a certain extent, the establishment and evolution of the common Eurasian Union market for goods and services helps absorb shocks affecting mutual investments, thereby mitigating the negative impact of economic contraction over the past two years: A partial absorber but not a panacea.

8. Challenges of real coordination of macroeconomic and monetary policies

It is crucial for EAEU countries to pursue coordinated macroeconomic policies. Doing so supports macroeconomic stability, contributes to the uniformity of principles governing the operation of the economy, and ensures that major economic indicators are coordinated to boost sustainability and deepen member states' economic integration.

A key EAEU development task is to secure full-scale coordination of macroeconomic policies, primarily monetary policy. In the long term, deepening integration in monetary policy may bring tangible benefits to the EAEU's three smaller economies, primarily by importing the economic stability generated by a reduction of long-term interest rates.

The EAEU Treaty stipulates the following three mandatory indicators (Table 6): debt-to-GDP ratio, inflation rate, and budget deficit. As of now, however, the EAEU does not have a clearly defined mechanism that could be used to enforce these criteria. This problem is still waiting for a solution. The Eurozone experienced a similar problem: criteria for sustainable sovereign foreign debt and budget deficits were defined and violated. As a result, due to the absence of strict fiscal policies and uncontrollable growth of public expenditures, debt growth took on dangerous proportions. This prompted a review of risk premiums and precipitated sovereign debt crises. The EAEU may now be facing a similar challenge. Over the year and a half since the Treaty's effective date, all three criteria have been violated by at least one of the parties. This is a very severe long-term problem that must be approached as soon as possible. The solution is likely to be complex: we need a "moral suasion" tool to pressure the parties into bringing their macroeconomic policies into compliance with the benchmarks defined by the EAEU Treaty.

A transition to new levels of monetary policy coordination is currently impeded by a host of persistent problems, including high and volatile inflation in some countries, sizeable dollarization of the economy, member states' use of

Table 6
Main criteria for determining the sustainability of economic development in EAEU member states.

Quantitative values of macroeconomic indicators		
Annual central government consolidated budget deficit ≤ 3% of GDP	Central government debt ≤ 50% of GDP	Annualized inflation rate ≤ 5 p.p. higher than in the member state where that indicator is the lowest

Source: EAEU Treaty.

different monetary regimes, and the high volatility of mutual exchange rates. In fact, these problems will shape the EAEU agenda for the next 5–10 years. They must be resolved regardless of whether member states need to deepen monetary policy coordination. A resolution to these problems will make it possible to reduce the costs of mutual trade and increase its volume, and open the way for sustainable growth in mutual long-term investments.

Top-priority steps in that area include reducing the level of dollarization and inflation in member states over similar long-term trajectories. Persistently high and volatile inflation complicates the implementation of monetary policy, as shocks have a more protracted effect on the real economy. The average inflation volatility in the EAEU is now more than 15 p.p. higher than in the EU in 1996–2000. For dollarization, its high level materially distorts monetary transmission and impairs the efficiency of monetary policies. This in turn boosts the probability of asymmetric shocks for the integration association.

In addition to the coordination of monetary policies, EAEU countries face some other challenges in the financial sphere: the liberalization of the banking sector, equalization of capital account regimes, liberalization of access to securities markets, and removal of restrictions on broker and depositary operations, etc. (Mishina and Khomyakova, 2014).

9. Network of free trade areas, trade and economic cooperation agreements

The Eurasian Union is planning to create a network of free trade areas (FTAs). The New Zealand FTA project was abandoned in 2014 in the aftermath of the fallout with the West. The first success story is the Vietnam FTA, which was ratified in November 2015. In 2016, the process gained momentum. It was not in vain that Kazakhstan's president proposed 2016 as the year of EAEU foreign economic policy. Why?

The first FTA of the Eurasian Economic Union

On May 30, 2015, in Kazakhstan, the EAEU and Vietnam signed an agreement establishing a free trade area (FTA), stipulating, *inter alia*, special operating procedures applicable to joint production facilities located in that country.

The document also envisaged a gradual mutual opening of the contracting parties' markets. By 2025, the average customs tariff rate in the EAEU will have declined from 9.7% to 2%, in Vietnam — from 10% to 1%. Import duties are slashed to zero for approximately 60% of mutual trade positions. Upon completion of a transition period, the share of zero-duty items will have increased to 88%. Russian Ministry of Economy expects trade turnover with Vietnam to double by 2020 (from $3.7 billion in 2014).

The set of documents signed by the parties contains an agreement *On a Special Regime for Russian Investors and Service Providers*, which specifically allows Russian companies to conduct business in Vietnam on the terms enjoyed by local firms. The agreement applies primarily to joint car-making projects and investments in power generation, transport infrastructure, and oil refining facilities.

Global trade rules are experiencing tectonic changes, which are very often prejudiced against EAEU countries. It should be admitted that today the EAEU — with its GDP of $2 trillion and a population of 182 million people (including 93 million gainfully employed people) — is not a self-sufficient market. It accounts for just 3.2% of global GDP. Any attempts to erect a "Eurasian fortress" are suicidal.

What are the possible solutions that can defuse the current crisis in relations between Russia and the West?

First, building up a network of free trade areas similar to the EAEU–Vietnam arrangement. Work is underway to negotiate FTA agreements between the EAEU and Israel, Serbia, and Singapore. Other potential partners include India, South Korea, Chile, Thailand, South Africa, and Iran (Table 7).

The EAEU's objective is to eventually negotiate a comprehensive treaty with its largest trade and economic partners — the EU and China. Long-term sustainable development is only possible if it relies on close cooperation with both the European Union and China (Vinokurov and Libman, 2012). There has already been some progress in that direction. The EAEU and China have started a dialog on a Trade and Economic Cooperation Agreement. The Eurasian Commission was granted the necessary legal mandate in June 2016. Discussions are underway regarding EAEU involvement in China's new strategic concept — the Silk Road Economic Belt. The prospects of mutually beneficial cooperation between the EAEU and China certainly give a powerful impetus to regional development and ongoing interaction with respect to transport, energy, and finance in Central Asia, Siberia, and the Far East (Karaganov et al., 2015).

There has been more interest in economic cooperation and integration between the EU and the EAEU. Deep economic integration with the EU is extremely important for the Eurasian Union. First, the EU is the largest trade partner for Russia and Kazakhstan: more than one half of the Russian Federation's trade volume is attributable to the EU; and Russia, in turn, is the European Union's third largest trade partner. Second, the EU could play the decisive role in modernizing the countries in the Eurasian integration project. In this light, the EU should also be regarded as a key long-term partner (Vinokurov, 2014). Naturally, we do not expect any rapid progress in our relations with the EU until the current profound crisis is defused.

Table 7
Ongoing work on EAEU trade and economic agreements as of November 1, 2016.

Active FTA	Vietnam (November 2015)
Negotiating mandates	China (mandate for a non-preferential treaty granted in May 2016) Iran Israel
Potential candidates (work teams, expression of interest, memorandums)	Egypt India Cambodia Mongolia (joint research group in operation) Peru Singapore Chile South Korea (joint research group in operation) New Zealand (advanced negotiations cancelled in 2014)

10. The common labor market — a tangible accomplishment

A discussion of the common labor market pales somewhat in comparison with a discussion of the common markets for goods and services. Nevertheless, it is precisely an area in which the Eurasian Economic Union has attained its most tangible results. Almost all barriers affecting workers from the Union's neighboring countries have been torn down, while the social guarantees enjoyed by the citizens of member states are now largely available to migrant workers and their family members. Member-state employers and entities contracting for work and services may hire workers from other member states without considering the restrictions present in their national labor markets. There are no licensing or quota compliance obligations (Aliev, 2015). Member-state workers do not require work permits. If migrant workers are "officially" employed, then their children attend kindergartens and schools, and all their family members have mandatory medical insurance coverage.

Due to its large size, over time the EAEU's common labor market may prove to be a significant positive factor contributing to economic growth of smaller economies. In particular, beneficial labor arrangements are crucial for long-term economic stability in Kyrgyzstan and Armenia (Tarr, 2016).

Implementation of the aforementioned regulations has suffered from a a number of obstacles and hindrances, but on the whole, the common labor market is already working. The list of major unresolved problems is topped by the technically complex issue of pension mobility. After all, each country has its own pension system. A special agreement is being designed to address that issue. The fact that the labor market is up and running is confirmed by the first available statistical data: in 2015, the number of Kyrgyz migrant workers in Russia increased by 1.6%, while the number of Tajik migrant workers decreased by 13.7%.

11. Public opinion

The broad public is generally supportive of Eurasian integration. According to public opinion monitoring conducted by the Eurasian Development Bank since 2012 as part of the *EDB Integration Barometer* project, public approval ratings of the Eurasian integration project within the EAEU range from 46% (in Armenia) to 81% (in Kyrgyzstan). Thus, a representative survey conducted in May–June 2016 showed that EAEU approval ratings in Kyrgyzstan, Kazakhstan, Russia, and Belarus are rather high at 86%, 74%, 69%, and 63%, respectively (Fig. 2). Conversely, in Armenia the level of support for the country's involvement with the EAEU has dropped to 46%. This may have been caused by the escalation of the Nagorno-Karabakh conflict at the time the survey was taken, but other interpretations are also possible (EDB, 2016).

Any interpretation or comparison of these figures with *Eurobarometer* data should allow for the influence of certain factors. People are truly supportive of the idea of Eurasian integration. This is true for the younger generation (18–30 year-olds): their support for Eurasian ideas is lower than that of the older generation but is still quite high. It should be noted, however, that people in Russia, Kazakhstan, Belarus, etc. support the Eurasian Union "in advance", focusing on ideas rather than the practical implementation of those ideas (at least for now). In the European Union, *Eurobarometer* figures are much more modest. Standard

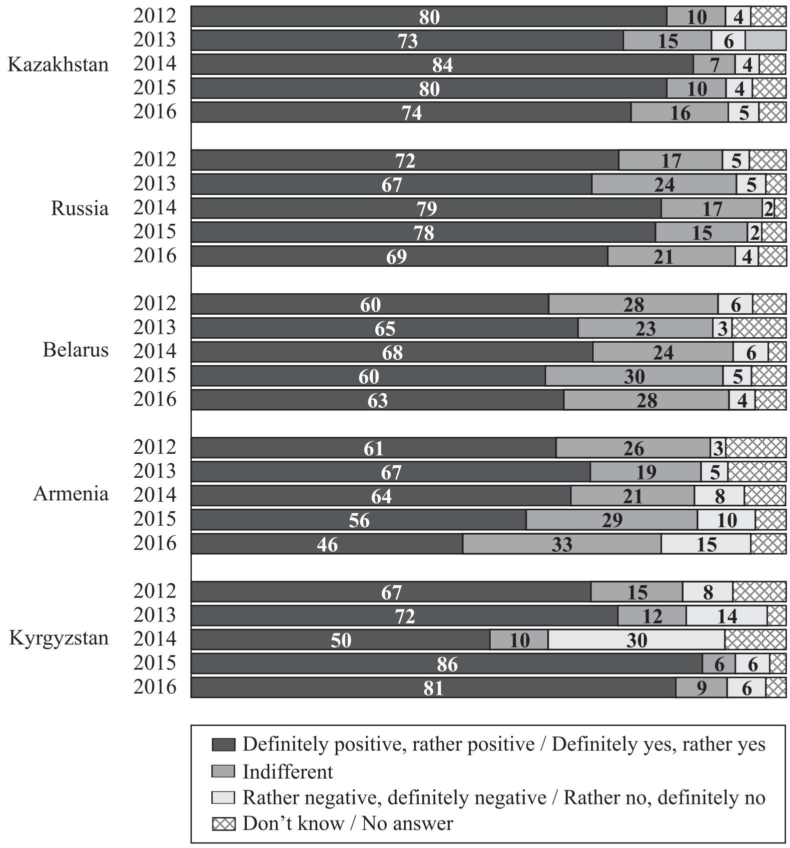

Fig. 2. Dynamics of public perception of the EAEU, 2012–2016.

Note: Question: Five countries have decided to create the Eurasian Economic Union (in essence, a single market for the five countries). What is your attitude towards that decision?
Source: EDB (2016).

approval ratings fluctuate within the 50–55% range, largely because Europeans consider the specific long-term realities of the European integration project. Still, the public's overall favorable attitude towards Eurasian integration creates a generally positive background and establishes confidence needed for implementing integration policies.

12. Conclusion

The EAEU is a new reality of the post-Soviet space. Its successes and stumbling blocs should be realistically assessed. While the direct comparison to the European Union can be misleading, it also makes more to access the EAEU on a somewhat smaller scale. In this regard, it is comparable to other general-purpose regional integration organizations, in particular customs unions or free trade areas—NAFTA, MERCOSUR[6], Cooperation Council for the Arab States of the Gulf, and the South African Customs Union.

[6] See Gómez-Mera (2013) on continuing trade conflicts within MERCOSUR—something that the EAEU is likely to experience in the coming years.

On the one hand, the Eurasian Economic Union is not a perfect "success story" worthy of being quoted in textbooks. After an initial phase of rapid growth, it may have hit a short-term ceiling by 2016. Much time may be necessary to break through that ceiling. On the other hand, it has achieved much and is quite viable. Its founding treaty and its institutions are working. The same applies to the common labor market. There is some progress in the development of common technical regulations (a total of 36 such regulations have been finalized to date). Integration effects will be maximized by realizing existing plans in these areas and implementing some more specialized initiatives (pertaining to, for instance, infrastructure, industrial policy, the agricultural and industrial complex, labor market, a single pension space, and research and education cooperation).

The EAEU is best viewed as a functioning customs union with a rich additional agenda. It features its own successes and stumbling blocks. Its structural characteristics are actually not unique. Economic domination by Russia? South Africa's weight in the South African Customs Union is even greater; the US dominates NAFTA. Raw materials account for the overwhelming share of total exports? Oil means even more for the Cooperation Council for the Arab States of the Gulf; MERCOSUR exports also have a pronounced bias toward raw materials. Nascent trade and economic conflicts within the Union? The history of MERCOSUR, ASEAN, NAFTA, and other regional integration organizations is replete with such conflicts. In a word, both the EAEU's achievements and its limitations are "normal".

The EAEU is a new reality for the investor community, too. A common market has been created in the territory of five states — a market that makes it possible to work from almost anywhere. Despite the existing imperfections in the Union's operating mechanics, it has already become a functioning common market with a relatively defined development roadmap.

The topics we have covered are consistent with several exceptionally important EAEU agenda items for the immediate future (approximately the next 5 years):

- The top priority is to complete the work aimed at creating common markets for goods and services and eliminating existing exemptions. In doing so, it is critical that the alignment of the Common Customs Tariff be maintained at a high level.
- The second task is to continue to methodically eliminate/unify the hundreds of remaining NTBs — from goods certification rules to special importer status.
- The third task is to efficiently coordinate macroeconomic (and particularly monetary) policies. Without such coordination, the "economic fabric" of the nascent integration association may unravel.
- Finally, it is necessary to forge numerous free trade areas and trade and economic cooperation agreements. This applies to two key trade and investment partners. The first is China. A favorable political background for a Sino-Russian agreement has already been created, and the work has begun in 2016. EAEU policies may realistically be aligned with Chinese *Silk Road Economic Belt* policies. Doing so will require negotiation and promotion of a common stance on infrastructural mega-projects and a detailed discussion of a Trade and Economic Cooperation Agreement between the EAEU and China. The second key partner is the European Union. In this instance, the only option available for the time being is a preliminary expert evaluation. Real progress will become possible only after the current political crisis is resolved.

References

Aliev, S. (2015). Labor migration in the Eurasian Economic Union. *Evraziiskaya Ekonomicheskaya Integratsiya, 4* (29), 65–74 (In Russian).

Alpysbaeva, S., Kenzhebulat, M., Kamzin, A., & Kaskeev, S. (2015). Structural changes in mutual trade between Kazakhstan and Russia against the background of external shocks and monetary policy differences. *Evraziiskaya Ekonomicheskaya Integratsiya*, *2* (27), 41–51 (In Russian).

Dragneva, R., & Wolczuk, K. (Eds.) (2013). *Eurasian economic integration: Law, policy and politics*. Cheltenham, UK, and Northhampton, MA: Edward Elgar.

Dutkiewicz, P., & Sakwa, R. (Eds.) (2014). *Eurasian integration—the view from within*. London: Routledge.

EDB (2015). *Monitoring of mutual investments in CIS countries 2015* (Report 32). St. Petersburg: Eurasian Development Bank, Center for Integration Studies.

EDB (2016). *EDB integration barometer–2016*: *Fifth wave of the survey* (Report 40). St. Petersburg: Eurasian Development Bank, Center for Integration Studies.

Gómez-Mera, L. (2013). *Power and regionalism in Latin America*. Notre Dame: University of Notre Dame Press.

Hamilton, D. S. (Ed.) (2014). *The geopolitics of TTIP: Repositioning the transatlantic relationship for a changing world*. Washington, DC: Center for Transatlantic Relations.

Hancock, K. J., & Libman, A. (2016). Eurasia. In T. A. Boerzel, & T. Risse (Eds.), *The Oxford handbook of comparative regionalism*. Oxford: Oxford University Press.

Karaganov, S. (Ed.) (2015). *Toward the Great Ocean 3: Creating Central Eurasia. The Silk Road Economic Belt and the priorities of the Eurasian states' joint development*. *Valdai Discussion Club Analytical report*. Moscow: Valdai Discussion Club (In Russian).

Kuznetsov, A. (2014). Russian direct investments as a factor of Eurasian integration. *Voprosy Ekonomiki, 8*, 58–69 (In Russian).

Libman, A., & Vinokurov, E. (2012). *Holding-together regionalism: Twenty years of post-Soviet integration*. Basingstoke: Palgrave Macmillan.

Mishina, V., & Khomyakova, L. (2014). Integrated currency market of the Eurasian Economic Space and home currency settlements: Myth or reality? *Voprosy Ekonomiki*, *8*, 41–57 (In Russian).

Tarr, D. G. (2016). The Eurasian Economic Union of Russia, Belarus, Kazakhstan, Armenia, and the Kyrgyz Republic: Can it succeed where its predecessor failed? *Eastern European Economics*, *54* (1), 1–22.

Vinokurov, E. (Ed.) (2010). *Eurasian integration indicators system*. Almaty: Eurasian Development Bank (In Russian).

Vinokurov, E. (2014). Mega-deal between the European Union and the Eurasian Economic Union. *Rossiya v Globalnoi Politike, 5,* 189–194 (In Russian).

Vinokurov, E., & Libman, A. (2012). *Eurasian integration: Challenges of transcontinental regionalism*. Basingstoke: Palgrave Macmillan.

Vinokurov, E., & Libman, A. (2014). Do economic crises impede or advance regional economic integration in the post-Soviet space? *Post-Communist Economies*, *26* (3), 341–358.

Vinokurov, E., Demidenko, M., Pelipas, I., Tochitskaya, I., Shymanovich, G., Lipin, A., & Movchan, V. (2015). *Estimating the economic effects of reducing non-tariff barriers in the EEU* (Report 29). St. Petersburg: Eurasian Development Bank.