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INTERNATIONAL COOPERATION IN THE BALTIC SEA REGION

CURRENT PROBLEMS IN RUSSIAN-LATVIAN RELATIONS

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Current relations between Russia and Latvia are still influenced by a series of mutual claims that appeared after the demise of the USSR. Latvia — as well as Estonia and Lithuania — is both an EU and NATO member state. However, unlike the above mentioned countries, its relations with Russia are developing at a more pragmatic level. Numerous political differences often result in economic losses both for Latvia and Russia. Despite the fact that Latvia has been an independent state for more than 20 years, there are still some unresolved issues in its relations with Russia. Today, relations between the two countries are often viewed through the prism of EU — Russia relations. Nonetheless, they often do not fit this context. Settling differences between Latvia and Russia will contribute to trade relations, which are increasingly important for both parties. In order to prevent and localise emerging conflicts, diplomats, politicians, and experts should interpret Russian-Latvian relations in view of the national features without referring to theoretical models based on the mythological "unity" of the three Baltic States.

Key words: economic problems, Latvia, economy, Russiaт influence, economic cooperation, transport and energy projects, international relations

Research on the history of the Baltic States and their relations with Russia in the context of contemporary global international politics seems to be relevant from the historical, political, and economic points of view. The need for such research relates to the changes that have taken place on the geopolitical map of Europe over the last 25 years. Three countries of the Baltic Sea region — Latvia, Lithuania, and Estonia — seceded from the USSR

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and, in the 2000s, acceded to NATO and the EU. It is worth noting that the economic policy of Latvia has developed in accordance with the EU Lisbon Strategy aimed at creating a knowledge-based competitive economy capable of stable growth, offering more quality jobs and ensuring better social coherence and environmental protection [1]. The selection of such a path of economic development is explained, first of all, by the fact that the country aspired to accede to the EU (earlier, the reorientation towards economic ties with the West was announced). Latvia submitted an application for the EU membership as early as 1995; the application acceptance meant that approval of the country's accession if the country met the EU's criteria.

As early as 1999, the Integration Commission started to operate in Latvia; its objective was to assess the readiness of the country for the accession to the EU. In 2002, it was acknowledged that all countries assessed by the Commission, including Latvia, did meet the EU requirements. The accession to the EU had an undoubtedly positive effect on Latvia's economy. According to the new EU budget, Latvia will receive 3,004 euros per capita, thus ranking third among the EU member states and fourth in terms of the share of support in the GDP (3.37%) [2].

However, in this new position, the Baltics — including Latvia — do not enjoy full sovereignty, part of which (that relating to the economy and politics) was delegated to the EU leadership. This fact cannot but affect the development of relations between Russia and the Baltic States, which are considered now in the light of EU — Russia interconnection, whereas the military and political issues are dealt with in the context of Russia-NATO contacts.

However, this situation exists only in theory. In practice, Russian-Baltic relations are often taken out of this context. "Latvia's foreign policy has a strong anti-Russian element. However, it is not a result of its international obligations. Latvia is a member of the EU and it is Latvia's sovereign choice. Russia's economic ties with Poland and Finland, Germany and Italy are more efficient and dynamic. NATO membership is also Latvia's choice; nevertheless, Russia's relations with Norway and Canada, Turkey and even the USA are clearer and more logical" [3]. This statement requires a comment. Russian-Latvian relations are far from being perfect, but they are much better and more pragmatic than Russian-Lithuanian and, moreover, Russian-Estonian relations. A number of factors, some of which will be considered below, make it possible to cautiously speak of the prospects for the improvement of Russian-Latvian relations.

When discussing the processes taking place in Latvia's politics and economy at the time, one cannot but focus on the period that affected the country's current condition. It is important to stress that after independence the new orientation towards deindustrialisation and deagrarisation of the national economic was not chosen consciously, nor set out in any document. This process was rather spontaneous and was accompanied by the closing of many large factories across the country, for example, the State Electrotechnical Factory (VEF), and the Riga Autobus Factory (RAF). The agricultural crisis was less pronounced but affected the non-urbanised districts thus extending its geographical scope. These trends resulted in a rapid increase in the unemployment and inflation rates. At first, it was inevitable; the economic indices plummeted throughout the post-Soviet space, and Latvia was no exception. Later the country's leadership placed emphasis on the banking

sector and logistics, which had to become the driving industries of Latvia's economy; however, it cannot be considered a fully justified decision. At the time, the economic boom was supported by direct investment from the West, which continued over the first years of the new millennium.

When reviewing the first years of Latvian independence, it is important to mention that in 1992—1993, the transition from a planned to market economy, which commenced when Latvia was a Soviet republic, was continued. Since this process was gradual, some economic sectors (trade, services, and banks) were exempt from governmental control; however, in other sectors (education, healthcare), such control persisted over a long time.

In our opinion, the key economic reforms were carried out in Latvia promptly and efficiently even before 1994 [4]. These are the currency, public utilities, healthcare, and municipal reforms. As to the currency reform, Latvia used the rouble as main currency until 1993. The national currency — the lat — was introduced in spring 1993; it replaced all circulating currency towards summer. Before that, the Latvian rouble was equated to the ecu: 200 Latvian roubles = 1 ecu; the exchange rate for the lat was 1 lat = 200 Latvian roubles, i. e. 1 lat = 1 ecu. Later, by 2005, the lat was pegged to a currency basket: the US dollar, the German mark, the Japanese yen, the British pound, and the French franc. Since 2005, the lat has been pegged to the euro. By spring 1994, the strict monetarist policy of the Central Bank of Latvia reduced the inflation rate to 37% in comparison to 109% in 1993. The processes of public property privatisation and its transfer to the previous owners (after the nationalisation of 1940) was not a rapid one. Factories and kolkhozes were transformed into cooperatives collectively owned by the employees. The number of privately owned enterprises was gradually increasing (in 1997, they accounted for 60% of the GDP). Many of them established partnerships with investors from other countries, especially, Sweden, Germany, and Poland. In 1994 and 1995, the economic reforms yielded first results. Almost a ten-year-long GDP decrease slowed down in 1993; in 1994, it began to grow. By 1994, the ownership of more than half of all agricultural lands was transferred to farmers and the rest to cooperatives. The privatisation of urban property was less rapid; certain problems resulted from the restitution practices.

The entrepreneurial abilities of population and the assistance of western countries also contributed to the rapid overcoming of the crisis resulting from the severance of economic ties forged in the framework of the Soviet economic complex. In order to mitigate the consequences of the rise in prices, the government established the minimum wage and supported the underprivileged, although the income of urban population remained quite low (in 1997, the income of 66% of the population was below the poverty line). As early as 1997, a 6.5% GDP increase was registered, however the inflation rate remained at 8.5%. The production growth slowed down in 1998 as a result of the Russian economic crisis nevertheless achieving the level of 4.5%, whereas the inflation rate decreased to 3.5% (one of the lowest levels throughout Eastern Europe).

The United Europe became the leading trade partner, which was significant support for the gradual development of the economy. Nevertheless, the hopes associated with the establishment of the customs union of Latvia, Lithuania, and Estonia did not come to fruition. However, this structure had at least some meaning before 2004.

The economic ties with the CIS states (especially Russia and Belarus) were also developing. Latvia's membership in the IMF and World Bank ensured the necessary investment and facilitated foreign trade.

It is worth noting that, at first, the leaders of the Soviet Baltic republics and, later, independent Baltic States were very cautious in their statements about the prospects of economic development and stressed the need to maintain economic relations with Russia [5, c. 27]. The Concept of the republic's economic accountability adopted shortly before the collapse of the USSR did not give an objective assessment of the country's potential. The claims against the Soviet leadership pertaining to excessive energy capacities in the conditions of current energy efficiency seem to be uncalled for. As G. A. Stanchinsky stressed [6], before independence, most of the Baltics' population were of the opinion that they were feeding Russia. After independence, it became clear that the higher standards of living were ensured in the republic trough the disproportional distribution of resources. So, for example the 1 t of meat/10 t of forage ratio, when converted into the world prices, turned out to be overvalued one and a half times. The transition to reciprocal payments at world prices had a negative effect on the condition of Latvia's import and export, this effect can be estimated at 821 million roubles (pre-inflation prices) [7].

In the first years of the 21st century, Latvia's economic growth approached a two-digit value. The term 'Baltic tigers' was coined to characterise the three Baltic states. The notion of 'Baltic tigers' was borrowed by historians from the economic vocabulary in the beginning of 2008. For the last time before the crisis, an increase in GDP was registered in the first quarter of 2008 (0.8%), whereas a decrease was observed until the second half of 2010. In the first quarter of 2009, Latvia's GDP decreased by 17.8%, in the second one by 18.1%, in the third by 19.1%, in the fourth by 16.8% [8]. During the economic crisis, the unemployment rate approached 19%. Latvia's banking system turned out to be disorganised and endured only due to the following factors:

1) governmental support;

2) the policy of Swedish banks that treated their Latvian assets as first priority (after Swedish assets);

3) the IMF's bailout loan of USD 7.5 billion, which accounted at the time for approximately 25% of the country's GDP.

At the moment, Latvia's economic performance looks almost perfect for Euro-integration. Latvia's government debt reduced to 40.7% of the GDP in 2012 against the limit of 60%. In 2013, the inflation rate in Latvia is expected at 1.4%, which is well below the 2.7% limit. Latvia's accomplishments are evident even against the background of the other Baltic States.

Latvia also meets the criterion of stability of exchange and long-term interest rates. Latvia's budget gap accounted for 1.2% of the GDP in 2012, the same gap is expected in 2013, which is twice as little as the 3% limit imposed by the Maastricht Treaty [10]. However, according to a number of leading experts, Latvia's economy lacks stability, whereas the monetary regulation methods have exhausted themselves [11]. It is well understood by many Latvia politicians. Latvia's Saeima approved the bill on the introduction of the euro as a new currency of the republic. Most members of the Saeima supported the adoption of the project drawn up by the Ministry of Finance. However, out of 94 members of the Parliament, 40 op-

posed the introduction of the euro and two abstained [27]. For the first time, no parliamentary group demonstrated unanimity. The law was submitted to the president and came to force only after his approval. The final decision on Latvia's accession to the Eurozone will be made by the EU ministers of finance after a debate at the European Parliament and the Council of the EU, though most experts believed that it would happen in July 2013.

The inflation rate in the Baltics according to Eurostat, 2001—2012,% [9]

Country	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012
Latvia	2.5	2.0	2.9	6.2	6.9	6.6	10.1	15.3	3.3	– 1.2	4.2	2.3
Lithuania	1.6	0.3	– 1.1	1.2	2.7	3.8	5.8	11.1	4.2	1.2	4.1	3.2
Estonia	5.6	3.6	1.4	3.0	4.1	4.4	6.7	10.6	0.2	2.7	5.1	4.2

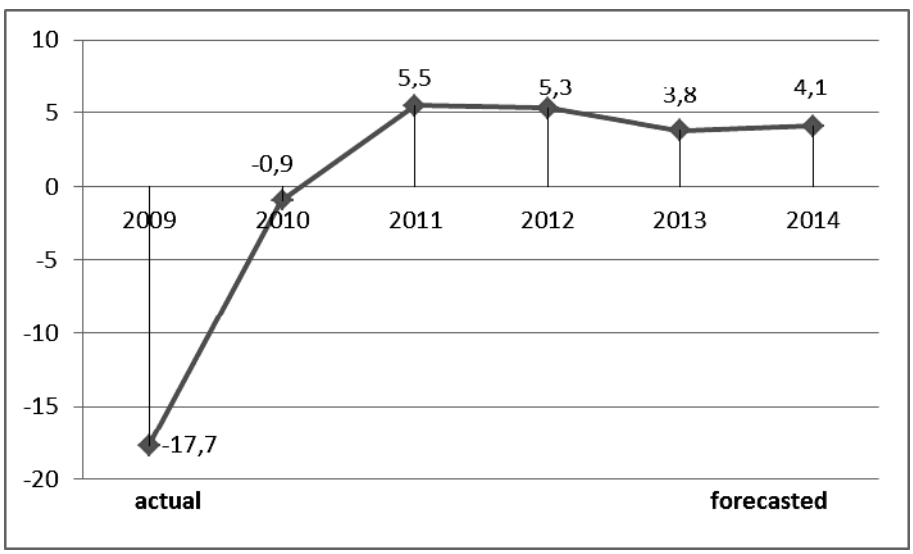

Fig. The dynamics of Latvian GDP in 2009—2014 [12]

Modern researchers stressed the aspiration of Latvia's leadership to accede to the EU "whatever the cost, even at the expense of crucial economic components such as the increase in internal competitiveness, the stimulation of national investors, and the support for the national producer and exporter" [13].

The negative consequences of the above were as follows:

- The transformation of the social policy resulted in a greater number of social problems, poorer social security, and mass migration of residents of all nationalities;
- As a result of attracting foreign investment, 70% of national production facilities were transferred into foreign ownership;
- Foreign consumption loans increased Latvia's debt, which, however, did not reach a critical level.

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Latvia has been an independent state for more than 20 years. However, there are still certain unresolved issues in relations with Russia. First of all, it is that of the Russian-speaking population having no Latvian citizenship. Moreover, the issue of the acknowledgement of the occupation of Latvia by the Soviet Union and Russia's liability (also economic) for the past events, which is often revisited by the Latvian party, does not contribute to the improvement of relations between the neighbours.

The collapse of the Soviet Union, the loss of the large Soviet sales and resource market, as well as the opening of borders, made Latvian industry uncompetitive. These circumstances led to the closing of a number of large enterprises, which pre-Soviet Latvia was famous for (a good example is VEF). However, some enterprises of all-Union significance survived in the harsh market conditions, one of them is the Riga Railcar Factory (RVR).

In the creation of an independent economy, emphasis was put on transit services alongside the banking sector. In the case of Latvia, transit accounts for 90% of the total cargo handled at ports [14, c. 3]. This figure changes from year to year by several points, but its economic meaning remains the same. In Latvia, transit accounts for 12.3% of the country's gross domestic product. Only trade and the manufacturing industries account for a greater share. A ton of transit cargo brings the Latvian economy 10 lats, therefore, 60 million tons bring 600 million lats [15].

A similar situation is observed in the case of Latvian railways. Their economic feasibility depends only on transit. In 2012, Latvian Railways managed to exceed the earlier volume of cargo transportation and reach the level of 60.6 million tons. Latvian Railways (Latvijas dzelzceļš (LDz)) paid almost 83 million lats in taxes in 2012, which is almost 8 million lats more than in 2011 [16]. More than 8% of Latvia's working population is involved in transportation and transit cargo handling [17].

At the same time, one cannot say that the opportunities for transit development have been exhausted. For example, there is a programme for the development of the Freeport of Riga for 2009—2018. This fundamental document covering almost all aspects of the functioning and development of the port hardly mentions any prospects for economic relations with Russia but includes cooperation plans with Kazakhstan and China [18].

From our point of view, Latvia has an optimal geographical position for developing transit relations with Russia; if this circumstance is supported by political actions of the leadership of the two countries, Latvia can obtain a significant additional financial resource.

The new opportunities for Russian-Latvian political relations opened up on October 13, 2006, when the Russian Minister of Economic Development and trade, G.O. Gref, and the Latvian Minister of Economy, A. Štokenbergs, signed an agreement on economic cooperation and the creation of an intergovernmental commission on trade and economic, research and technological, cultural and humanitarian cooperation.

The legal framework for the functioning of the intergovernmental commission and economic relations in general was developed quite rapidly. The out-dated Russia-Latvian intergovernmental agreement on the principles of trade and economic relations concluded as early as 1992 was terminated by mutual consent.

In October 2006, a meeting between the Latvian Prime Minister, A. Kalvītis, and V. Putin took palace in Finland. It is worth stressing that Kalvītis stands out as one of few Latvian high-profile politicians who are convinced that Latvia should have normal relations with Russia and who managed to establish relations of trust with the Russian leadership. The conversation with Putin gave a green light to the process of boundary treaty ratification initiated by the heads of corresponding commission in the late 1990s. The treaty about the Russian-Latvian state border was signed by Kalvītis in Moscow in March 2007, ratified by the Saeima in May and by the State Duma and the Federation Council in September of the same year.

The economic relations between Russia and Latvia have developed quite smoothly since 2006. A decrease in Latvia's and Russia's GDP as a result of the world crisis diminished interest in further cooperation and the search for new areas thereof. Traditional transit remained the basis for the connections between the states. However, one cannot overlook the fact that the Latvian authorities demonstrated political foresight having prevented political provocation relating, for instance, to the relocation of the monument to the Soviet liberators in Tallinn. As a result, transit via Estonia decreased and that through Latvia grew [19]. It is worth stressing that the forecasts of Russian politicians who believed that, in 2013—2015, Russian transit via the Baltic ports would cease, are not likely to become a reality.

As of February 22, 2012, the Latvian register of enterprises (Uzņēmumu reģistrs) listed 3301 joined Latvian-Russian enterprises. Russia invested 206 m into businesses registered in Latvia (according to Lursoft). The largest Russian investors in Latvia are:

- Transnefteproduct — 36.55 m (34% of the shares of LatRosTrans — pipeline transportation, steam and hot water supply);
- The Moscow City Property Department — 20.09 m (92.55% of the shares of AMO Plant — an affiliate of the Russian motor vehicle manufacturer AMO ZIL);
- Gazprom — 13.57 m (34% of the shares of Latvijas Gāze — gaseous fuel production, treatment, and transportation via distribution pipelines
- The Commercial Bank of Moscow— 10.82 m (99.87% of the shares of AO Latvijas Biznesa banka — monetary intermediation);
- Russian banker Igor Tsyplakov — 10.82 m (100% of the shares of Rigensis Bank);
- Yuri V. Shefler — 7.9 m (100% of the shares of Meierovica 35 — accommodation services) [20].

The number of banks with Russian capital increased to five. The possibility of opening an affiliate of Sberbank in Riga is being discussed [21].

Trade relations between Latvia and Russia are playing an increasingly important role for both parties. A good example is the working visit of the Russian Minister of Industry and Trade, D.V. Manturov, to Latvia, in the course of which he took part in the burial of a time capsule at the construction site of a railway carriage manufacturing factory of the Russian UralVagonoZavod group in the town of Jelgava. It seems to be of importance that the President of Latvia, A. Bērziņš, the Russian ambassador to Latvia, A.A. Veshnyakov, and

the Metropolitan of Riga and All Latvia Alexander took part in the ceremony [22]. In other words, a large business project turned into a major international political event.

The international trade of Latvia was estimated at 15.595 billion lats in 2012 [23], which is 13.7% over the 2001 figure. Latvian exports reached 6.898 billion lats in 2012—15% over the 2011 figure. At the same time, imports totalled 8.697 billion lats in 2012—12.7% over 2011. Latvia's major export partners are Lithuania, Estonia, Russia, Germany, Sweden, Poland, Denmark, and the UK. All in all, the EU states account for 69.3% of Latvia's exports. Latvia's major import partners are Lithuania, Germany, Russia, Poland, Estonia, Finland, and Belarus. The EU states account for 77.2% of Latvia's imports [24].

According to the official data [25], Latvia is the Baltic leader in mutual trade with Russia. The data of the Federal Customs Service suggest that, in 2011, the trade turnover increased by 22.4% as compared to the previous year and reached USD 8.1 billion, whereas exports totalled 7.2 billion (a 24.7% increase) and import 0.8 billion (a 1.5% increase). Russia's surplus in trade is stable and amounted to USD 7.3 billion. In the first quarter of 2012, the positive dynamics persisted. The export structure is dominated by mineral commodities — diesel fuel, fuel oil, natural gas, coal (88%), chemicals (4%), metals (mostly, flat steel; 3,4%), and vehicles (1.7%). The import structure is dominated by electric appliances (27.9%), foodstuffs and agricultural supplies (25.7%), chemicals and pharmaceuticals (12.2%), and textiles (3.9%). Experts estimate that Russia-Latvian mutual trade can reach approximately USD 9 billion in 2012 and exceed the pre-crisis value.

To sum up, one can arrive at the following conclusions:

- The diplomatic component of Russian-Latvian relations is much greater than that of Russian-Estonian and Russian-Lithuanian ties. Mutual understanding rests not only on economic relations. Right-wing parties do not dominate in the Republic of Latvia; political coalitions succeed each other with rapidity, the civil society is critical of politicians — in these conditions, Latvia's foreign policy has to 'adapt' to the averaged social and political views.
- At the moment, Latvia's economic policy rests on taking full advantage of the Euro-integration opportunities and underestimating the potential of cooperation with Russia.
- High GDP growth rates can be ensured in the years to come by balanced Russian-Latvian relations.
- Despite understanding the need for good-neighbourly relations with Russia, Latvian leadership is rather inconsistent when it comes to intergovernmental relations.
- Bilateral relations in the conditions of global economy cannot be fully balanced. Latvia declares the need for independence from Russian energy supply. "Such dependence is increasingly interpreted in Latvia, Lithuania, and Estonia as the last thing connecting these countries to the Soviet past" [26]. However, the dependence in the transport and energy fields is a two-way phenomenon. Latvian — as well as Russian — politicians should take into account that, in the conditions of global division of labour, political and economic interdependence in such small region as the Baltic one is the rule rather than the exception.

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