

## **Russia and Europe – is there a new opportunity?**

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There is no denying that we are meeting to discuss the issue of relations between the Russian Federation and the European Union at a difficult time.

Behind you is the election to the Duma last Sunday.

All over Europe, the headlines have reported the assessment of the International Observation Mission, with Mr Bruce George, President of the OSCE Parliamentary Assembly, stating here in Moscow two days ago that “the main impression of the overall electoral process is of regression in the democratisation process in Russia.”

And these headlines come after months dominated by the waves generated in the international debate by the arrest of Mr Mikhail Khodorkovsky in Novosibirsk in the early morning hours of October 25.

Having spent last week in discussions in both Brussels and Washington, I can only say that the way in which Russia is discussed in policy circles in these and other capitals today is different from what was the case only months ago.

I'm saying this because I believe it is important that this is fully understood here in Moscow. There might be the understanding or polite words here and there, but they do not adequately reflect the reality of a shift in sentiment on the issue of Russia in the last few months.

The question is whether there has been a change in the direction of the development of Russia, and the consequences this then would have for the overall relationship.

We here today all belong to those that are committed to developing a deeper, more enduring and mutually beneficial relationship between the Russian Federation and the European Union, thus facilitating not only the continued modernisation of Russia but also the long-term political stability and economic vitalisation of all of Europe.

But we must understand that our task looks more challenging and more difficult now than it did until fairly recently. It will require firm political will, as well as statesmanship, on both sides to carry the process forward in the years ahead.

Tomorrow evening, the heads of state and government of the 25 present and soon-to-be members of the European Union starts gathering in Brussels for a critically important meeting of the European Council. In focus is the question of the new Constitutional Treaty that will define the federation of nation states that the Union to a very large extent already is.

Next year will be a year of transition and transformation for the European Union.

With the ten new members coming in on May 1<sup>st</sup>, a new Treaty of Rome in all probability being signed shortly thereafter, elections to the new European Parliament in all these 25 countries June 10 – 13 and thereafter the nomination of a new President of the Commission and a new Commission to take responsibility for driving the process of integration forward during the rest of this decade it is truly a watershed year that lies ahead.

In addition, there will start negotiations on a new multi-year financial framework for the Union. And towards the end of the year, the European Council will take the critically important decision on whether to initiate membership negotiations with Turkey.

This will happen at same time as it assesses progress in the ongoing negotiations with Romania and Bulgaria and discusses the application already there from Croatia as well as the application likely to have been received by then from Macedonia.

During this year of transition and transformation, I would expect the political energies of the European Union to be focused primarily on these transitions and transformations.

But in spite of this, the issues of relations with what are referred to as Wider Europe as well as the Russian Federation will continue to attract attention. An assessment of the situation is likely to be made. After the large enlargement now happening, this is no more than a natural development.

Next year will also be a year of transition in other important respect.

Here in Russia, it is only after the presidential election in March that it will start to be possible to form a better opinion on which policies are likely to be pursued by Russia in the coming years. And on the other side of the Atlantic, there will be an almost constant election campaign from the first primaries in January up to the ballot itself in the beginning of November.

But while waiting the outcome of these different transitions, we should be aware of the dangers of the relationship deteriorating. If I listen to some voices from Russia, there is even the risk of a game that might endanger the Cooperation and Partnership Agreement between Russia and the European Union that is the basis of the relationship. And the events of the last few weeks have demonstrated the risks of crisis and political confrontation in the different weak regions bordering both Russia and the European Union.

We must thus concentrate on avoiding these problems, at the same time as we focus on the potential for structural improvement in the relationship that is there the coming year of transition, transformation and uncertainty.

It is then - in 2005 – that a new European Commission will be firmly in place, and we will now more about the future of the Constitutional Treaty as well as about future membership prospects. It is then that we will also know much more than we know today about where Russia is really heading. And it is then that a new or a renewed administration will be in

place in Washington, affecting the relations with the European Union as well as with the Russian Federation.

During this coming year, both the European Union and the Russian Federation must seek more coherent answers to some fundamental questions.

Is the European Union truly ready to become a strategic actor of consequence in this Wider Europe, in the Greater Middle East, in Africa and in other areas of obvious interest? The groundbreaking European Security Strategy that will be formally adopted by this European Council does establish the roadmap for, but the proof of the pudding remains in the eating.

The answer to this question will, needless to say, be of major importance also for the relationship with Russia.

Is Russia ready to continue to pursue reform policies that will make a commitment to cooperation and integration with the rest of Europe more than just empty words, including the rule of the law, a political system that is more democratic and less managed and a commitment to an open and competitive economic system?

The answer, particularly after the last events, is by no means an obvious one.

If there is an affirmative answer by the European Union to its question, and by Russia to its, I believe we will be entering a new era with big potential for cooperation and integration, ultimately to the benefit both of the stability of our common continent and the economic and social well-being of all its citizens.

If both were to fail, prospects are likely to be bleak in both these respects. We might see tension bordering on conflict in different parts of the wider defined wider Europe, and we will see the economic development of Russia restricted to an increasing reliance on exports of its abundant natural resources, primarily oil and gas, but ultimately unable to generate the domestic and foreign investment necessary for a true modernisation and broadening of its economic base.

At the upcoming meeting of the heads of state and government, the European Union will adopt a common European Security Strategy, thus paving the way for the Union to become a more active, more coherent

and more capable actor when it comes to the different security issues that we are all facing.

In particular, the European Security Strategy highlights the threats posed by terrorism, by the spread of weapons of mass destruction as well as all the problems arising out of fragile, failing or failed states, and seeks to chart the development of the different policy instruments needed to address these.

The European Union has created, and seeks to extend, a zone of stability, the rule of the law, good governance and democracy on and around our continent. First and foremost this is done by the integration of the member states of the Union itself; a task that becomes increasingly demanding as the Union expands. But we will see it giving more focus on issues of good governance, stability and the rule of the law in the wider Europe beyond its immediate boundaries.

Here, it is obviously in the interest of the European Union to develop a partnership with the Russian Federation, as well as to seek an active role for the United States whenever appropriate. But such a partnership – desirable as it is - will only be possible if there is a sufficient degree of commonality of interests and values. And it will only be possible if there is a mutual recognition of that fact that it is only by acting together that we can find stable solutions.

In this respect, there have been mistakes on both sides.

Over Kosovo in early 1999, the Western countries thought that they could achieve a political solution without the full participation of Russia. This failed, we got a war, and we have since then not been able to return to the search for a peaceful solution to the issue.

Over Moldova recently, Moscow repeated the same mistake, believing that a political settlement could be engineered by Russia alone without involving other key international actors. This collapsed, and we are left with a continued situation in Moldova which risks becoming a burden on the region as well as on the relationship between Russia and Europe.

In Georgia, we should all be aware of the risks. There are forces in Georgia clearly looking to the United States and Europe for support, and there are forces equally clearly looking to Russia for support.

If there is not the constructive coming together of the key international actors, the only result that is certain is the fracturing of the country with long-term consequences that are likely to be worse for those areas and countries more adjacent. Increased instability in this area is most unlikely to be in the interest of Russia.

The European Union and Russia should have the same interest in the stability of these areas that constitute their common "near abroad". Fully respecting the choices these countries might make themselves, it should be in our common interest to avoid the type of mistakes I have mentioned, and develop a closer partnership on these issues.

This common interest obviously extends to other areas as well. Nearly all the heroin on the streets of Moscow, and more than three quarters of all on the streets of the rest of Europe, originates in conflict-ridden Afghanistan. If we fail to bring stability to that country in the years to come, it will affect not only the vulnerable countries of Central Asia, but our own societies as well.

Both Russia and the European Union borders the area often referred to as the Greater Middle East. While it used to be said in the past that the Balkans started beyond the suburbs of Vienna, the Middle East today might well be seen as starting in the suburbs of Paris, London or Moscow. In this city alone, the Muslim population is said to be in the order of two million people.

Our interest in the resolution of the conflicts of this region is thus profound.

That the European Union and Russia has managed to work together constructively within the so-called Quartet can be said to testify to this. And in the post-Saddam reality of Iraq, we both have a profound interest in the evolution of a country where the territorial integrity is respected, the rule of law and representative government is established, and which does not become a source of rivalry, tension and possible even terrorism. In all these respects, our interests today are essentially the same as those of the United States.

I thus see the possibility of developing a strategic partnership between the European Union and Russia on all these issues to the obvious benefit of both of us. With the European Union step by step become a more active, more coherent and more capable actor, this partnership should have a profound potential.

But as this is said, it must be pointed out that there is an obvious risk of things developing in another direction. When Russia found itself isolated at the recent ministerial meeting of the OSCE in Maastricht on the important issues of Moldova and Georgia, it led to profound question marks for the future. It is important that these are straightened out, in a constructive way, as soon as possible.

At the recent EU-Russia Summit in Rome, an attempt was made to identify what was referred to as four common policy spaces for the future.

The first was the concept of a Common Economic Space, which has been around for two years without making much progress.

The second was the common economic space of freedom, security and justice, with much to be done. The important issue of visas belongs in this category.

The third was the common space of external security, which I have just referred to.

And the fourth is a common space of research, education and culture, where some notable progress has been achieved, notable in the space sector, but the potential obviously is much greater.

It is not without reason that it is often the economic issues that are in focus.

Without being fully a part of Europe and the world, Russia will never be able to rise out of the poverty and despair after its seven tragic decades of tyranny and isolation. And without a Russia able to overcome this horrible legacy, our common efforts at stability will be much harder to achieve. All of Europe has a profound interest in a Russia that is strong and stable and confident in its future.

A century ago, Russia was one of the fastest growing economies of the world. The industrial revolution was beginning to transform the country. St Petersburg and Moscow were bustling European metropolitan centres. From Sweden, we saw artists and entrepreneurs moving East to the rising nation of Russia.

It is worth noting, that had this development continued, Russia today might have been with the United States and other parts of Europe in the top of the world as concerns economic development. But instead, it lingers near the bottom of the league of the countries of the industrial revolution a century ago.

Unavoidably, Russia will continue to pay the price for the seven decades of communism for decades to come. But the big question is whether it will remain essentially a petroeconomy trying to shield itself from the outside world in other areas, or whether it will truly try to make the leap towards a modern, broadly-based and competitive economy.

From a European point of view, it is somewhat bizarre that China is a member of the World Trade Organisation, but Russia is not. Without a membership of the WTO there are bound to be limits on the amount of economic integration between the European Union and Russia, while at the same time the Russian economy will be at the mercy of the laws of the jungle in the international marketplace.

A target has now been set for concluding the negotiations between Russia and the World Trade Organisation before the end of 2004. Russia must push aside the protectionist interests that are trying to limit its integration with the rest of the world, a formulae must be found on the issue of market-conform pricing of natural gas and Russia must also recognize that recent events might have made the mood in the US Congress somewhat more difficult to handle on this issue.

The concept of a common economic space has never been properly defined, and has thus remained a formula without much of operational meaning. I believe the main reason for this is the policy muddle that has kept Russia outside of the WTO for too long. Without this membership, it is hardly possible to discuss the steps towards first a true free trade area and then possible beyond this that otherwise would be logical.

Part of the policy muddle that has restricted progress has been the uncertainty surrounding the economic relationships between the CIS states. Although the one ambitious scheme after the other has been launched, it is difficult for an outside observer to see much structural progress on these issues either. The net result of the different schemes with the CIS label has thus tended to be to brake the progress towards the WTO and to limit the potential for development of the common economic space with the European Union.

Obviously, all of these issues need to be resolved. But first things must come first, and the WTO membership should obviously be given priority. In the coming year of transition in Europe, the issue must still remain very much on the table of the goal of completed membership negotiations in 2004 should be met.

Although Russia has moved somewhat from its overdependence on the export of oil and gas during the last decade, it remains essentially a raw material-exporting economy. Much of the improvement in economic performance during the last few years have come as a result of the combination of the success of the new Russian oil companies in turning around a decaying old Soviet oil industry with increasing production as a result and the high oil prices we have seen.

To which extent these factors will continue to apply remains to be seen. Increasingly, there will be the need for vast investments in exploration as well as the exploitation of new, remote and expensive fields. What we have seen so far has been a turn-around of the old decaying Soviet oil industry, with the next necessary phase far more demanding not the least in terms of capital.

In the long-term much more important field of gas, developments are obviously lagging behind. We have seen some reforms, but the essence of the old structure is still in place. Here as well, there will be the need in the years ahead to move forward with gigantic investments in order to open up new fields, as well as large investments in the infrastructure needed to export this gas to the hungry markets of Western Europe, China and Japan.

In the debate during the past months there have been voices calling for these natural assets to remain under some sort of state and national control and even ownership. This is certainly an option, but it should be recognized that it is in all probability an option that will limit the room for expansion of these important industries in the years ahead. Without capital and technology from also other countries, the rate of expansion will clearly be less than it otherwise would have been.

From the European point of view, these are issues of importance. I believe that the European Union will be increasingly dependent on the supply of natural gas from Russia in the decades ahead. There are alternatives – Norway, North Africa, LNG – but they are either not sufficient or would over time be even more expensive than the Russian option. From both the political and the economic point of view, an

economic and energy partnership between the European Union and Russia is the best alternative.

But the big questions for me are not linked to the course that Russia will take with its oil and gas industries in the years to come – important as these are.

The critical question is whether one would truly move beyond a petroeconomy and develop into a broadly based competitive modern economy. It is if this course is chosen that we see the truly large potential for integration and cooperation across all of Europe opening up.

The recent meeting of the EU-Russia Industrialist Round Table here in Moscow painted a rather gloomy, but I believe correct, picture of the overall situation.

The Round Table said, that “notwithstanding evident successes in economic growth and some institutional reforms, the systematic risks of investing into the Russian economy remain high. The major structural, legal and institutional reforms are not completed or effectively implemented... Despite improvements in sovereign rating due to high oil and gas revenues, Russia remains at the very bottom of the international investment ratings and the total volume of direct foreign investment is abysmally small compared to the scale of the Russian economy and its potential.”

And it went on to note, that “for the last decades the country essentially did not replenish its productive capital assets and is now facing structural crisis and technological catastrophes in many areas. The modernisation of the Russian industry and the reconstruction of its vast infrastructure will require enormous investments which can not be fully financed from domestic sources. The investment climate and related issues of institutional and structural reform remains the key to the high and sustainable rates of long-term economic growth in Russia.”

It is in my opinion by addressing these issues that Russia can move from just a petroeconomy to gradually becoming a modern economy that can fully be part of the economic integration and cooperation in Europe. The benefits should be enormous both for Russia and for the rest of Europe.

Whether this will be the course pursued in the years to come remains to be seen. I started by indicating the question marks that have appeared during the last few months. But I believe it is important to understand that

the key to the potential of integration and cooperation between Russia and the European Union lies in the reform process in Russia itself.

To the list of the four common spaces identified at the summit in Rome ought, in my opinion, to be added a fifth common space of common commitment to the development of democracy, respect for the rule of the law as well as human rights. Although Russia as well as the members of the European Union are committed to these values by our membership of the Council of Europe, the reports coming out of the observer missions for the Duma election clearly points towards a room for continued discussions.

Over time, there is a link between the economic and the political system in a country. Whether this is old Marxism or not, I do believe it is correct. And while a petroeconomy can certainly be combined with a semi-authoritarian political system, the development of a broadly based, modern and competitive economy hardly can.

We have seen authoritarian and semi-authoritarian regimes in different parts of the world developing up to a certain level, but beyond a certain level of development the need for a firm rule of the law, a transparent and open political system and a vibrant society also outside the spheres of the state and the dominating economic units creates the need for a fully-fledged democratic system.

Thus, the choice for Russia between a petroeconomy and a modern, broadly based economy is not only a choice of long-term economic potential, as well as possibilities of integrating and cooperating with the rest of Europe, but also over time a choice of political regime.

I belong to the generation that was brought up during the decades of the Cold War, the wall in Berlin and the communist system extended by the powers of Soviet arms deep into the hearth of Europe. But I also belong to the generation that has been fortunate to see the true historical miracle of the peaceful dissolution of this empire based on occupation, the liberation also of Russia and the demise of the confrontations of the past..

The task of our generation is to build a new system of security, cooperation and democracy encompassing as large parts of our continent as possible.

Gradually, we are through the European Union building a federation of nation states that will include all of Europe to the west of Russia and the Ukraine, stretching eventually from the Arctic Ocean to the Mediterranean, over time in all probability including Turkey as well.

This is by no means an easy, smooth or uncomplicated process. Nothing like this has ever been done. And we are the best half the way towards fulfilling that agenda that history threw upon us through the big changes of 1989 and 1991.

The transformation of Russia from a decaying rustbelt covering 11 times zones to a modern European democracy, bordering on China and exposed to all the turmoil's of the Greater Middle East, will obviously take its time. But it remains as crucial a part of the building of our new Europe as does the need to keep and reinforce the relationship across the Atlantic with the United States.

Whether also Russia will one day decide to seek membership of our federation of nation states is an open question to be decided by Russia itself. My belief is that a country the size of Russia will find it hard to accept that sharing of sovereignty across a very wide range of issues that is the essence of what we are trying to do. But that decision is yours to take – not ours.

I started out by saying that we are meeting to discuss this subject at a difficult time. There are question marks in the outside world concerning the direction of Russia. There is an understandable difficulty here and elsewhere to understand all the complicated working of the European Union and its transformation. And we are all affected by the new security challenges and threats identified not the least by the new European Security Strategy.

For the time being the task is to prevent a deterioration of the somewhat strained relationship we are seeing today. This will be particularly important during the months of transformation and transition ahead of us during the coming year.

But thereafter, we all should have an interest in reforging and strengthening the relationship. If Russia is willing, I'm sure that the European Union will be eager. But there are choices to be made on both sides in order to make this possible.

