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# THE GEOGRAPHY OF THE EURASIAN ECONOMIC UNION: FROM CHALLENGES TO OPPORTUNITIES

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## Geography of the Eurasian Economic System

The defining feature of the economic system of Eurasia is its geography. In fact, the region can be defined as an ‘area of inaccessibility’. For instance, it is home to the Dzungarian depression, the most remote area from the coast (2,645 kilometers away from the nearest ocean). This continental ‘pole of inaccessibility’ lies not far from the borders of China, Russia, Kazakhstan and Mongolia — the last two themselves landlocked countries.

In terms of access to infrastructure and altitude above sea level, Eurasia’s continental pole of inaccessibility is also located in China: “the Qangtang plato in Northern Tibet, to the south of Przhevalskogo Ridge.”<sup>1</sup> The nearest settlement is 500 kilometers away.

The Eurasian Economic Union (EEU) has a unique geography not only in regional, but also global terms. Armenia is the only country

Tajikistan rank third and fourth in the world among landlocked countries with the highest elevation, after Bhutan and Nepal.

Overall, Central Asian countries form one of the world’s largest groups of landlocked countries. Uzbekistan is the only country in the world, apart from European ministates, separated from the sea by one or more countries.

Russia has the longest land border in the world and is unrivaled in the world in terms of the number of poles of inaccessibility.<sup>4</sup> Of all EEU countries Russia is the only one that is not landlocked. However, since most of its territory is far from the coast, in certain respects Russia is even more continental than its Eurasian integration partners.

Climate is also an important factor. Russia is the second coldest country in the world after Canada (with an average temperature of  $-5^{\circ}\text{C}$ ). Only three countries in the world, Canada, Russia and Mongolia, have a negative average temperature. In addition, 55 to 65 percent of Russian territory, according to various estimates, is in the permafrost zone. Out of its 67 ports only 19 operate year-round, and seven of them are located in Russia’s Far East.

The eminently continental nature of EEU countries is further emphasized by the distance separating their capitals from the coastline. For example, capitals of Central Asian countries are a long distance away from the coast. Moscow and Kiev are the two most inland capitals in Europe, and Minsk is in the top five.

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### The Eurasian Economic Union has a unique geography not only in regional, but also global terms

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in Western Asia<sup>2</sup> that lacks access to a major body of water (Azerbaijan has access to the Caspian Sea). Belarus is the largest landlocked country in Europe. Kazakhstan is the largest landlocked country in the world<sup>3</sup>, while Kyrgyzstan and

<sup>1</sup> Korolyov, A., 2013, ‘Polyus nedostupnosti Rossii kak ekologicheskyy etalon dikoy prirody’ [Russia’s ‘pole of inaccessibility’ as an environmental wildlife standard], *Vestnik Udmurtskogo universiteta*, vol. 4, p. 106.

<sup>2</sup> Under a UN definition, Western Asia includes the Middle East and Trans-Caucasian countries.

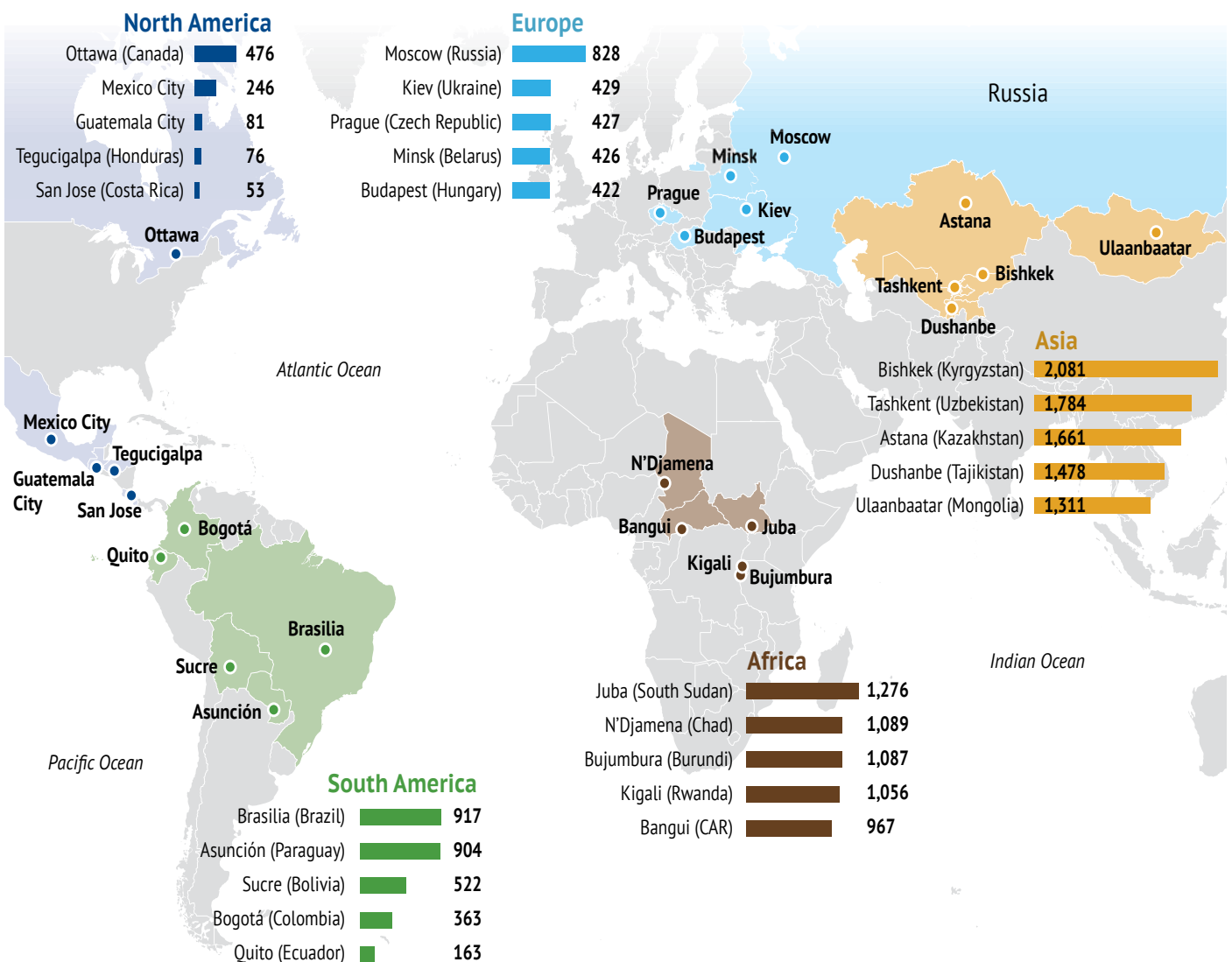
<sup>3</sup> Given the uncertainty of the Caspian Sea’s status and the fact that it is not connected to the world ocean, Kazakhstan is viewed by the UN as a landlocked country.

<sup>4</sup> Korolyov, A., 2013, ‘Polyus nedostupnosti Rossii kak ekologicheskyy etalon dikoy prirody’ [Russia’s ‘pole of inaccessibility’ as an environmental wildlife standard], *Vestnik Udmurtskogo universiteta*, vol. 4, p. 109-110.

The remoteness from the sea coast, as well as pronounced infrastructure and population gaps across the Eurasian economic space create a set of unique obstacles to economic development. This primarily has to do with low factor mobility, as well as limited agglomeration effect and economies of scale within the economy. At the same time, this creates opportunities for preserving

the unique environment. Considering also the strategic advantage of having vast remote areas and abundant natural resources, Eurasian countries are uniquely positioned to promote economic development. However, their potential can be hardly unleashed without properly assessing and exploring ways to overcome challenges the EEU faces due to its geography.

FURTHEST INLAND CAPITAL CITIES BY CONTINENT, KM



## Eurasia's Macroeconomic Development

Of the 193 countries in the world, 43 or about 20 percent are landlocked, and among those the share of underdeveloped countries is much higher compared to the global average. In fact, 20 of the 54 least developed countries (LDCs) are landlocked, compared to just 3 out of 35 high-income countries. It should be noted that landlocked Western European countries benefit from proximity to major trade partners, river trade routes and developed transportation infrastructure.

Contrary to expectations, the share of transport costs in product prices has not decreased. On the contrary, the reduction of tariff barriers over the last several decades of globalization, as well as non-tariff barriers in some regions, has pushed up the share of transport costs in overall import-export costs. Statistics for the last 15 years show that being landlocked affects economic development significantly<sup>5</sup>:

- *being landlocked reduces average growth by about 1.5 percent compared to maritime countries;*
- *on average, landlocked countries rely on IMF assistance longer than coastal countries;*
- *on average, GDP in landlocked developing countries is just 57 percent of the GDP of their neighboring coastal states;*

- *landlocked countries trade on average 30 percent less compared to coastal countries.*<sup>6</sup>

An extra distance of 1,000 kilometers raises costs by seven times more if the distance is overland than if it is maritime. The elasticities of transport costs with respect to distance are: 0.46 (by air), 0.39 (by rail), and 0.22 (by sea).<sup>7</sup> Research shows that costs of onetime border crossing correspond to transport costs for 4,000 kilometers of sea shipping.

Having analyzed foreign trade data for specific countries, Steven Radelet and Jeffrey Sachs found transportation costs to be about 50 percent higher for landlocked countries. There are also estimates showing that landlocked developing countries bear exorbitant transport costs with a ratio of up to 10–20 percent, compared with 4.7 percent for industrial countries and 2.2 percent for the United States.<sup>8</sup> According to the available data, doubling transport costs reduces foreign trade by about 80 percent.<sup>9</sup>

The early promoters of Eurasianism recognized that the distance issue was fundamental. “Those countries and regions, which due to their location mostly rely on maritime transport, are much less affected by distances in their international

<sup>5</sup> *The cost of being landlocked: logistics costs and supply chain reliability*; 2010, World Bank, Washington DC. Available from: <http://documents.worldbank.org/curated/en/620801468168857019/pdf/558370PUB0cost1C0disclosed071221101.pdf>

<sup>6</sup> Irwin, DA & Tervio, M, 2002, 'Does Trade Raise Income? Evidence from the 20th Century', *Journal of International Economics*, vol. 58, p. 1-18.

<sup>7</sup> Behar, A & Venables, A, 2010, 'Transport Costs and International Trade', in 'Handbook of Transport Economics', André de Palma, Robin Lindsey, Emile Quinet & Roger Vickerman (eds.), p. 11. Available from: <https://pdfs.semanticscholar.org/9c24/806fb476c7f6930207438966e0e6193260c6.pdf>

<sup>8</sup> *The cost of being landlocked: logistics costs and supply chain reliability*; 2010, World Bank, Washington DC. Available from: <http://documents.worldbank.org/curated/en/620801468168857019/pdf/558370PUB0cost1C0disclosed071221101.pdf>

<sup>9</sup> Vernon, HJ, Shalizi, Z & Venables, AJ, 2001, 'Geography and Development', *Journal of Economic Geography*, vol. 1, issue 1, p. 81-105.

and inter-regional exchanges compared to countries limited in their economic activity to transportation by land,” wrote Pyotr Savitskiy almost a century ago.<sup>10</sup>

This leads to high import and export costs. In a 1998 paper co-authored by Jeffrey Sachs<sup>11</sup>, the authors argue that a re-export model was extremely difficult to achieve in landlocked LDCs due to the higher cost of intermediate products.

According to Sachs, the disadvantage of landlocked countries has two aspects. First, coastal countries and regions can have an interest in creating additional costs for landlocked countries. Second, developing inter-state transport infrastructure is always more challenging than within a single country.

Consequently, landlocked countries face not only geographical and economic challenges, but also possibly political challenges that stand in the way of economic development.

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### Apart from hindering economic growth and undermining trade, being landlocked can also have some potential advantages

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At the same time, it would not be correct to view the landlocked status as a “geographical burden.” If anything, this shows the need to devise an economic development model for the region taking into account the country’s location. Apart from hindering economic growth and undermining trade, being landlocked can also have some potential advantages:

- *Continental alliances tend to last longer and usually evolve into strategic rather than tactical frameworks by catering to the core interests of the regional powers; without integration structures they would be unable to compensate for being far from international transport corridors. This shows the need to coordinate trade and economic policy. On the contrary, Brexit shows that maritime powers can be opportunistic when it comes to regional integration.*
- *Continental countries have broad possibilities to promote inter-regional cooperation, primarily in terms of cross-border cooperation (micro-regionalism).*
- *There is also the factor of interdependence in relations between continental countries, which not only makes them more eager to promote stable integration frameworks, but also increases the benefits from economic integration, with trade expansion accompanied by efforts to step up exports by overcoming spatial limitations.*
- *Opportunities to promote import substitution and develop domestic manufacturing or cooperation within a region due to high transport costs for imports from third countries.*
- *The possibility of building complimentary economies and agglomerations and benefitting from economies of scale by merging regional markets.*

<sup>10</sup> Savitskiy, P. 1997, 'Kontinent-ocean (Rossiya i mirovoi rynok)' [Continent-Ocean. Russia and the World Market], in 'Kontinent Evraziya. Evraziystvo' [Continent Eurasia. Eurasianism], Moscow, Agraf.

<sup>11</sup> Radlet S. & Sachs J.D. (1998). *Shipping Costs, Manufactured Exports, and Economic Growth*. Harvard University.

All in all, if the international experience in promoting economic development is any guide, continental countries can rely on two main approaches to overcome the challenges posed by their landlocked status. The first approach consists of signing regional and multilateral agreements aimed at facilitating trade and transportation of goods. The second approach would be to develop regional transport infrastructure in order to streamline access to maritime transport routes.

Eurasian theorists, primarily Pyotr Savitskiy, emphasized the importance of integration as a way to compensate for the remoteness from global markets. He wrote about “promoting economic complementarity of nearby continental regions and their inclusive development.”<sup>12</sup>

- *lowering customs duties and other barriers between countries in order to cut costs for reaching major ports and international markets;*
- *unifying and streamlining transport regulations in order to bring down the costs of delivering goods to coastal areas;*
- *pooling resources to finance construction and maintenance of joint transport corridors in coastal areas;*
- *creating conditions for establishing trade and economic ties between specific areas of countries within a regional group (micro-regionalism).*

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Eurasian integration and, primarily, efforts to promote cooperation within the EEU create new opportunities for Eurasia’s inland regions, and could facilitate their integration into global logistics chains and macro-regional projects

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What are the specific outcomes of regional integration that could help address the challenges of being landlocked? These include:

It should be noted that Eurasian integration and, primarily, efforts to promote cooperation within the EEU create new opportunities for Eurasia’s inland regions, and could facilitate their integration into global logistics chains and macro-regional projects, such as China’s ‘Belt and Road initiative’, the non-preferential agreement between the EEU and China and the initiative to create a Greater Eurasian Partnership (trade and economic agreements to align the agendas of the EEU, SCO and ASEAN). These initiatives could provide new opportunities for linking Eurasia’s inland regions to the coastal regions of Europe and Asia.

<sup>12</sup> Savitskiy, P, 1997, ‘Kontinent-ocean (Rossiya i mirovoi rynek)’ [Continent-Ocean. Russia and the World Market], in ‘Kontinent Evraziya. Evraziystvo’ [Continent Eurasia. Eurasianism], Moscow, Agraf.



## The Peculiarities of Eurasian Microeconomics

Let's now analyze the continental factor in the economic development of EEU countries in terms of macroeconomics. The producer exporting its goods usually bears the transport costs. As a result, corporate profits may vary substantially depending on the distance separating them from the coast. This assumption is confirmed for EEU countries when comparing logistics costs of major regional exporters with those of producers from coastal countries.

The shipping distance is a major factor when assessing a country's competitiveness. According to an OECD paper,<sup>13</sup> even though technological advances in transport and communications helped reign in transport costs, distance remains an important factor. For instance, a 10 percent increase

Railway transport accounts for 87 percent of cargo shipments in Russia, excluding pipelines, and exceeds 60 percent in Belarus and Kazakhstan, compared to less than 40 percent in the United States and about 15 percent in China. Overall, in coastal countries shipments are mostly handled by maritime transport.

Differences can be seen by comparing the cost of transportation per unit of production by sea and land. For example, freight costs from Australia to China stand at \$9 per ton, compared to \$22 per ton from Brazil, and transshipment at seaports costs \$2–4 per ton. In 2014, the railway tariff for shipments from Siberia to ports in Russia's Far East exceeded \$35 for coal and ore, \$100 for steel, while transshipment costs at Russian seaports stood at \$12–18 per ton.<sup>14</sup>

The substantial cost difference for sea and land transportation makes it harder for producers from EEU countries, where overland shipments dominate, to compete on the global market against companies from maritime countries. World Bank data show that the average cost

to export per container in EEU countries was equal to \$3,158 in 2014, twice the global average (\$1,560), and triple of the EU average of \$1,042. The only EEU country with a cost to export per container below the global average was Belarus (\$1,460), which is still approximately 30 percent above the EU average.

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**The substantial cost difference for sea and land transportation makes it harder for producers from EEU countries, where overland shipments dominate, to compete on the global market**

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in shipping distance reduces trade volumes by 10 percent. The study also suggests that distance has a major impact on economic development trends.

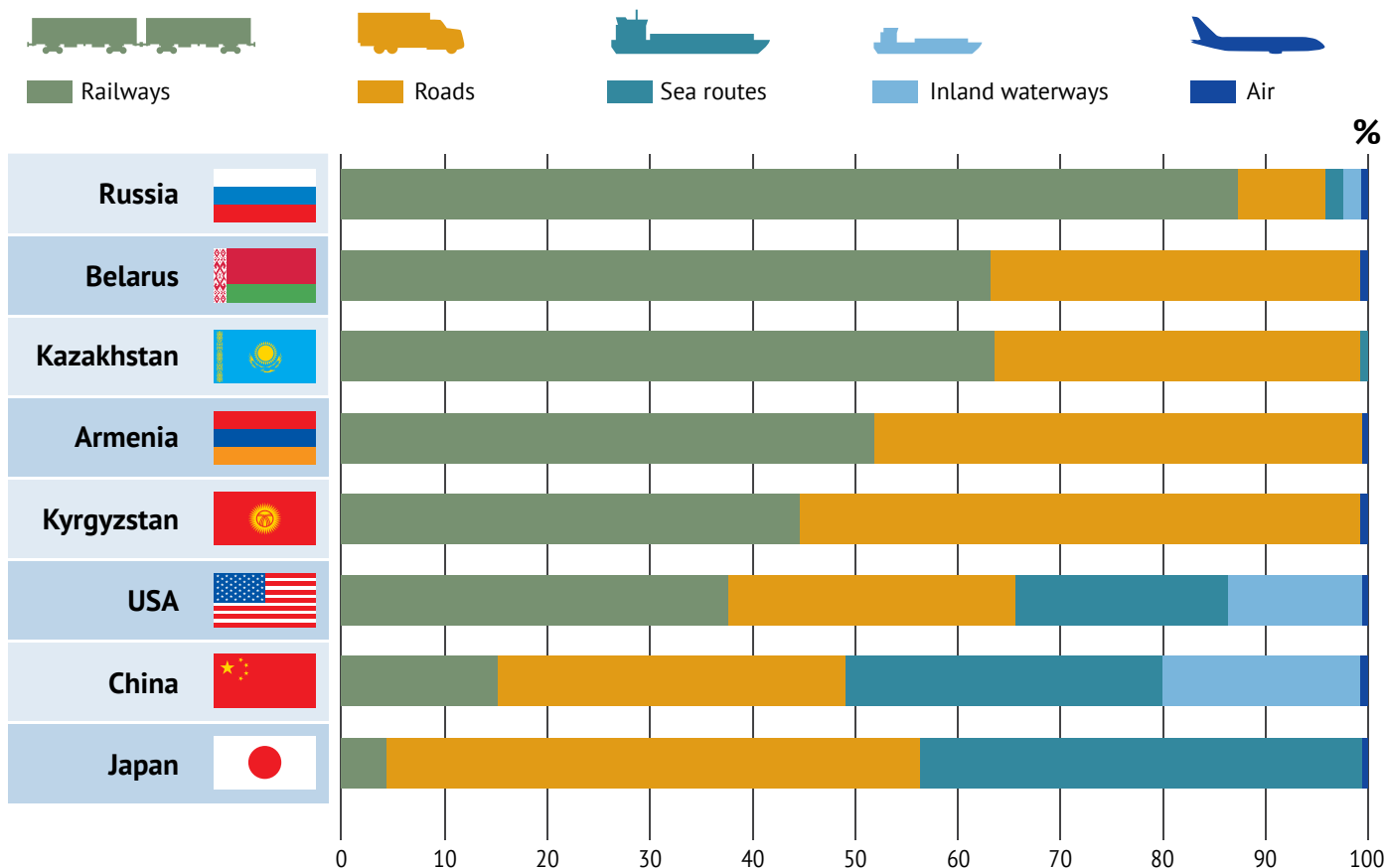
Railway shipments account for the bulk of cargo turnover in EEU countries, which is a major differentiator compared to other leading economies in the world.

<sup>13</sup> OECD 2008. *Economic Policy Reforms. Going for growth*. Available from: [http://www.keepeek.com/Digital-AssetManagement/oeed/economics/economic-policy-reforms-2008\\_growth-2008-en#page1](http://www.keepeek.com/Digital-AssetManagement/oeed/economics/economic-policy-reforms-2008_growth-2008-en#page1)

<sup>14</sup> Atnashev, M, 2015, 'Ne tol'ko neft': chto zhdet rossiiskuiu metal-lurgiiu' [Not only oil: what awaits the Russian metallurgy], Carnegie Moscow Center, October 13. Available from: <http://carnegie.ru/commentary/2015/10/13/ru-61592/ijpy>

## DOMINANT MEANS OF TRANSPORTATION BY COUNTRIES

As a share of total freight transport



\*Pipelines are not included

\*\*Figures for 2015 (Russia), 2012 (Japan), and 2014 (Others)

Source: Special Report, Eurasian Development Bank.

In the second half of the 20th century, many countries across the world transferred their manufacturing operations from inland areas to the coast. At the same time, the USSR massively shifted its industrial capacity inland, mainly driven by the relative isolation of its economy and the need to develop mineral deposits in Siberia and the Urals. The situation was further complicated by the fact that most former Soviet republics, including the current EEU countries, lost

access to the key year-round ports following the collapse of the USSR.<sup>15</sup>

This point is supported by a number of examples. Russia's ore mining complexes are located in continental Eurasia, far from major ocean ports. Exports from Mikhailovsky GOK iron ore mining and processing plant, which is part of Metalloinvest mining

<sup>15</sup> Bezrukov, L., 2006, 'Kontinentalno-okeanicheskaya dikhotomiya v mezhdunarodnom i regionalnom razviti' [Continental-oceanic dichotomy in international and regional development], abstract of a doctoral thesis in geography, Irkutsk.

company, are shipped to ports on the Black Sea (900 kilometers by rail) and Baltic Sea (1,200 kilometers by rail).

In comparison, the distance to the Indian Ocean for Australia's iron ore deposits is about 500 kilometers, while iron ore mines in Brazil are separated from the Atlantic Ocean by 500 to 900 kilometers of rail.

Russian coal travels one of the longest rail routes in the world, and the longest when exported, while the key competitors — Australia, South Africa, South America and Indonesia — all export coal by sea. For example, in Australia, the distance from a port to the most remote coal extraction site does not exceed 300 kilometers. In Russia, coal exports mostly originate in Kuzbass, with a shipping distance exceeding 3,500 kilometers. Even extraction in eastern Siberia and Yakutia would do little to reduce the gap in terms of transport costs. Consequently, transport costs still account for a substantial share of the overall cost at 50–60 percent for power plant coal and 30–40 percent for coking coal. In comparison, transport costs account for less than 10 percent of the overall cost in the oil industry, range from 10 to 20 percent in aluminum production, and are under 20 percent in the metals industry.<sup>16</sup>

All in all, coal shipments in Russia are unique in terms of the scale of the transportation leg, which is the least flexible portion of the overall costs and cannot be easily adjusted. According to 2016 data from Kuzbass Fuel Company, when export prices were at their

low of \$49 per ton, the producer earned \$8–9 after paying all the costs.<sup>17</sup>

This difference in transport costs affects corporate spending and competitiveness in meaningful ways. For instance, Metalloinvest ranks second in the world in terms of its iron ore deposits behind Brazilian Vale. Kazakhstan's ERG ranks seventh, behind Australia's BHP Billiton and Rio Tinto, as well as Cliffs Natural Resources and FMG in North America. Metals and iron ore markets mostly target China, which currently consumes almost one half of global iron ore exports. Although Russia and Kazakhstan are neighbors to the world's largest iron ore consuming country, taken together they account for a meager 1 percent of China's iron ore imports, while Australia accounts for 42 percent and Brazil for 14 percent.<sup>18</sup>

Ore from the Kursk Magnetic Anomaly has to cover 4,000–7,000 kilometers, depending on the specific route, by rail in order to reach the Chinese border. For Australian suppliers the distance by sea exceeds 9,000 kilometers, and Brazilian companies ship their products for almost 22,000 kilometers in order to reach Chinese ports. Despite their remote location from the key global iron ore consumers, Vale, BHP Billiton, Rio Tinto and FMG account for 72 percent of the global iron ore market. Metalloinvest sends 66 percent of its ore to the domestic market, exports 19 percent to European countries and just 10 percent of its output go to Asia.<sup>19</sup>

<sup>16</sup> Markova, V & Churashev, V, 2013, 'Put' ugliya' [Coal Way], *Expert Siberia*, no. 22 (377), June 3–10. Available from: <http://expert.ru/siberia/2013/22/put-uglya/>

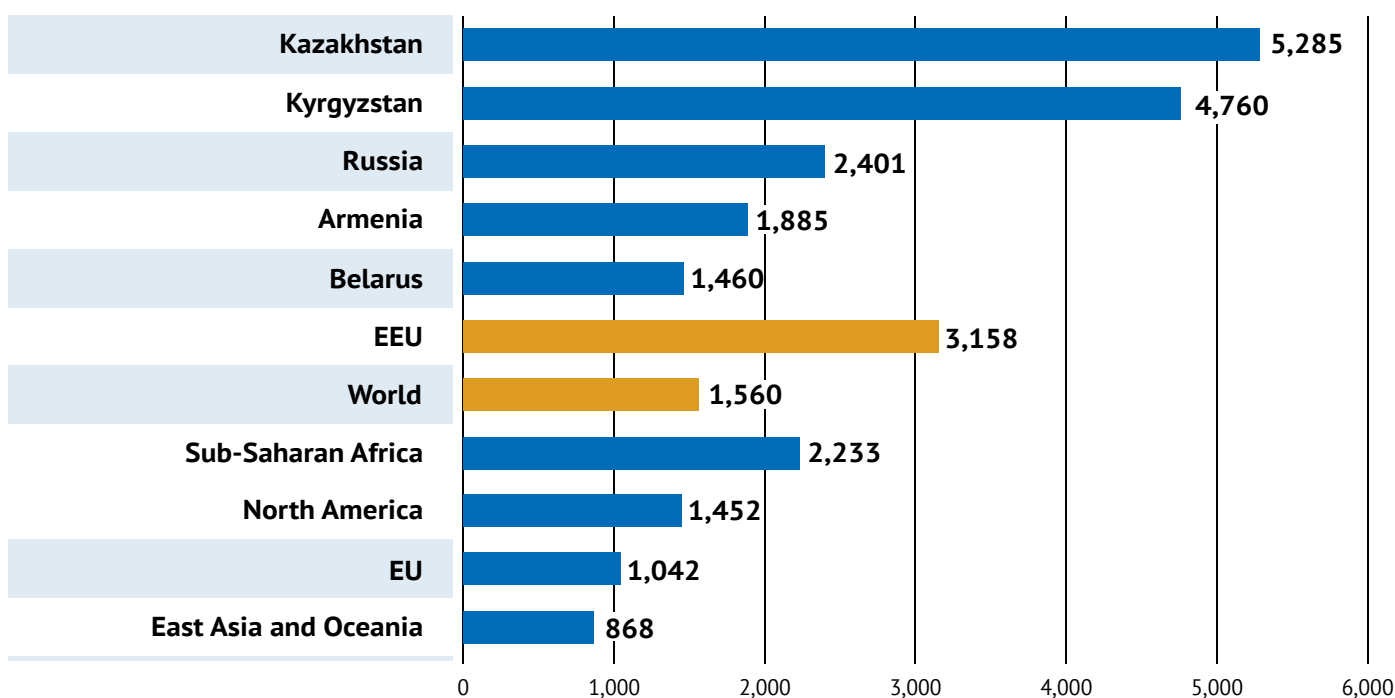
<sup>17</sup> EBRD *Industry Review*.

<sup>18</sup> Calculations based on UN *comtrade statistics*.

<sup>19</sup> *Metalloinvest Annual Report 2015*.

## EEU COUNTRIES TRANSPORT COSTS, 2014

## Average cost per container, \$



Source: Special Report, Eurasian Development Bank.

In the absence of an efficient transport and logistics system and given the dependence on overland shipments, being a neighbor to the world's largest market does not help Russia or Kazakhstan promote iron ore exports. Railway transport is a losing proposition compared to maritime shipments. According to calculations by The Journal of Commerce, it costs \$8,000 to ship a 40-foot container by rail from Europe to China, while shipping the same container by sea costs about \$3,000.<sup>20</sup>

<sup>20</sup> 'Okno v Evropu: kak Kitai zapustil novyi «Shelkovyi put'» v obkhod Rossii' [A Window to Europe: China Launches a New Silk Road excluding Russia], 2015, RBC, December 15. Available from: <http://www.rbc.ru/politics/15/12/2015/56703a6d9a7947f88a89ae7d>

Despite excessive supply on the Russian iron ore market (surplus of about 25 percent),<sup>21</sup> integration in the international market remains limited due to high transport costs. It costs about \$40 to transport one ton of iron ore from the Kursk Magnetic Anomaly to China.<sup>22</sup> The critical price point for Russian producers stood at \$67–70 per ton in 2013/2014, compared to \$45–50 for coastal producers.

<sup>21</sup> '«Dvoinoe dno» rynka zheleznoi rudy' [False Bottom of the Iron Ore Market], *Metallurgy Bulletin*. Available from: <https://www.metalbulletin.ru/analytics/ores/628/>

<sup>22</sup> Pomel'nikov, II, 'Sostoianie i perspektivy razvitiia zhelezorudnoi promyshlennosti v usloviakh «medvezh'ego rynka»' [Current State and Prospects for Development of the Iron Ore Production in the Bear Market Conditions], *Gornaia promyshlennost'*. Available from: <http://mining-media.ru/ru/article/ekonomich/8994-sostoyanie-i-perspektivy-razvitiya-zhelezorudnoj-promyshlennosti-v-usloviyakh-medvezhego-rynka>

## Case Studies of Switzerland, Belarus and Uzbekistan

What follows are three case studies, one from Western Europe, one from Eastern Europe and one from Central Asia, providing insight into risks and opportunities faced by landlocked countries.

### Switzerland

Switzerland is one of the most successful landlocked countries, at least as far as economic development is concerned. Its economic model is based on its unique development path, as well as regional and geographical factors that could hardly be replicated in other regions of the world.

Switzerland is a key European transit country offering a transport corridor that goes through the Alps and links the country to the coast along the Rhine, which can be navigated by sea vessels, including container ships. The Gotthard Base Tunnel opened in late 19th century, creating a rail link between northern and southern Europe.

Switzerland is an export-oriented economy. In 2015, exports accounted for 63 percent of the country's GDP. Of course, services make up a substantial share of exports (25–30 percent),<sup>23</sup> including financial services, where the country started building its competitive edge long before the 20th century.

Switzerland mostly trades with its close neighbors: EU countries account for 78 percent of its exports and 43 percent

of imports.<sup>24</sup> Apart from geographical proximity and well developed transport infrastructure, Switzerland and the European Union are linked by a free trade agreement, transit agreements, and have harmonized their legal frameworks to a large extent to reduce tariff and non-tariff barriers. In 2016, Switzerland officially withdrew its application to join the European Union filed back in 1992.

Switzerland lacks major energy reserves, which drives up production costs. At the same time, Swiss exports are dominated by products with high added value (chemical products, pharmaceuticals, cars, electronics, watches, etc.), which are less affected by commodity or transport costs.

Even though Switzerland backed away from joining the EU, it was still able to either substantially reduce or eliminate altogether tariff and non-tariff barriers by signing sector-specific agreements with the EU. That said, Switzerland's advantages are not limited to transport availability, value-added exports of goods and services, and EU trade agreements. A UN report on the development of landlocked countries points to the "very stable political climate" as a major prerequisite for Switzerland's development.<sup>25</sup>

<sup>23</sup> 'Trade in goods and services', 2016, OECD Data. Available from: <https://data.oecd.org/trade/trade-in-goods-and-services.htm#indicator-chart>

<sup>24</sup> 'Swiss Economy – Facts and Figures', 2017, The Federal Council, August 18. Available from: <https://www.eda.admin.ch/aboutswitzerland/en/home/wirtschaft/uebersicht/wirtschaft---fakten-und-zahlen.html>

<sup>25</sup> Trade, trade facilitation and transit transport issues for landlocked developing countries. Global event of landlocked developing countries and transit countries on trade and trade facilitation. URL: <http://unohrrls.org/UserFiles/File/Elle%20Wang%20Uploads/LLDCs%20Publication.pdf>

## Belarus

Just like Switzerland, Belarus has an export-oriented economy (exports account for 63 percent of GDP) with a high proportion of services exports (22.5 percent in 2016).<sup>26</sup> Belarus can be compared with other landlocked Eastern European countries that have an export-oriented economy, such as the Czech Republic, Slovakia, Hungary, etc. At the same time, since it is separated from key export markets by longer distances, transport costs for Belarus are 30 percent above the EU average (\$1,460 compared to \$1,042 per container). At the same time, Belarus is the only EEU country with transport costs below the global average of \$1,560 and more than two times below the EEU average of \$3,158.

Transport costs take on even greater significance, since heavy manufacturing (trucks, tractors), minerals and chemical products (potassium fertilizers, oil products, etc.) dominate exports and are mainly delivered by rail.

Belarus benefits from its human capital and developed transport infrastructure. It offers the shortest transit routes for linking EEU, CIS and Asian countries with Western Europe, as well as North-South routes linking Scandinavia, Baltic countries and Russia's north-west with Southern Europe.

Belarus also offers transport corridors connecting Russia to Baltic ports in Klaipeda, Ventspils and Riga. However, revenue from transit has been on the decline since Russia

decided to shift its exports to its own ports in the Leningrad Region. According to official statistics, transport corridors in Belarus are currently operating at 25 to 40 percent of their capacity.<sup>27</sup> Railway transport with its relatively high costs plays a key role in these transits. The track gauge width changes on the border with Poland from 1,524 to 1,435 millimeters, which also increases costs.

Russia and EEU countries are key trading partners for Belarus (more than 50 percent of foreign trade). The country also trades with Great Britain, the Netherlands, Ukraine, Lithuania, China, etc., which means covering longer distances compared to Switzerland, as well as relying on transit countries with which Belarus does not have trade deals or similar technical standards.

Although Belarus does not have any trade agreements with the EU, its countries account for about 25 percent of Belarus' foreign trade. Exports from Belarus are dominated by oil products, potassium fertilizers, crude oil, and semi-processed goods. Belarus relies on Latvian and Lithuanian ports to deliver most of its products to the EU and other countries (for example, China, Brazil).

Belarus is a member of the Eurasian Economic Union, benefiting from zero tariffs and lower non-tariff barriers on its main export market, where it delivers products with higher added value. As the EEU continues to eliminate bottlenecks and non-tariff barriers, and streamline customs procedures on its borders, Belarus is becoming

<sup>26</sup> 'Foreign Trade of Belarus in the first half of 2017', *Belarussian Ministry of Foreign Affairs*. Available from: <http://mfa.gov.by/export/>

<sup>27</sup> 'Transport in Belarus', *Belarus Facts*. Available from: [http://belarus-facts.by/ru/belarus/economy\\_business/key\\_economic/transport\\_and\\_communications/](http://belarus-facts.by/ru/belarus/economy_business/key_economic/transport_and_communications/)

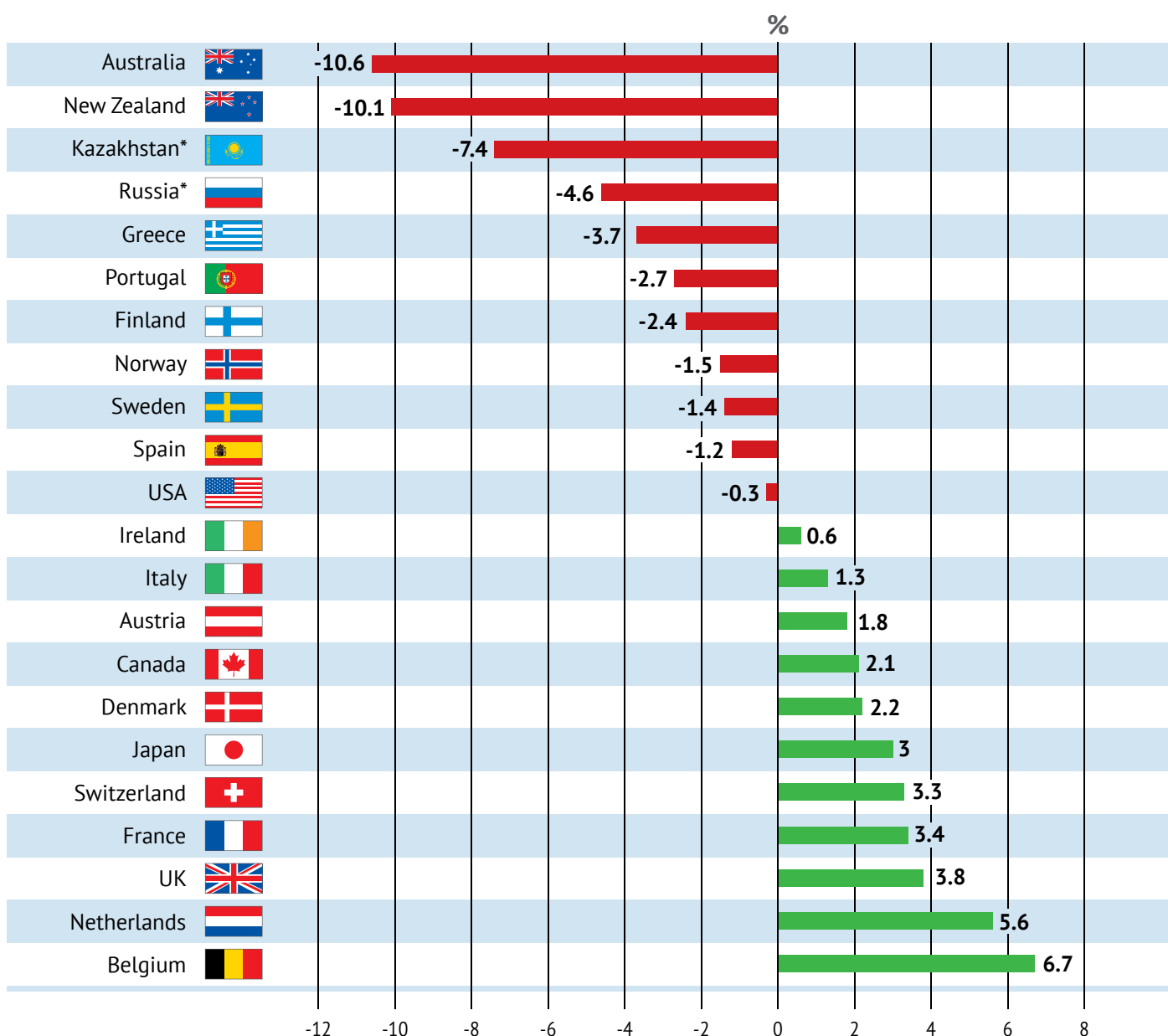
increasingly important as a priority transit country for overland trade corridors between China and Western Europe, taking into account, among other things, the political instability in Ukraine.

### Uzbekistan

Unlike Switzerland or Belarus, Uzbekistan is located in Central Asia, where all countries are landlocked. In fact, Uzbekistan is not

## ECONOMIC GEOGRAPHY PROS AND CONS

### How does the distance to market contribute to GDP per capita?



\*EDB estimate

Source: Special Report on microeconomics of the Eurasian geography, Eurasian Development Bank.

far from the global ‘pole of inaccessibility’, and is a unique country, since it is separated from the sea by more than one country (only Lichtenstein in Europe is in a similar position). The nearest high sea port is more than 3,900 kilometers away. Desert covers about two thirds of the country’s territory, and the main cities are located in river valleys.

Uzbekistan mainly exports energy resources, food, gold and cotton,<sup>28</sup> all of which are mostly transported by rail or road, which increases costs, considering the distance and the need to cross transit countries.

Uzbekistan operates within the CIS free trade area. However, non-tariff barriers remain substantial across Central Asia, compounded by persisting political disagreements between regional countries. Of all key trading partners, only Kazakhstan shares a border with Uzbekistan, while China, Russia, Turkey,

Switzerland and South Korea are all far away and can be reached only by land corridors by crossing many borders. Distance to the main European and Asian markets ranges from 4,600 to 7,000 kilometers, depending on the route, and the distance to the closest sea ports is 3,900 to 6,000 kilometers by rail.<sup>29</sup>

Uzbekistan produces energy resources on its own, and seeks to protect its market through import substitution. In the post-Soviet era, Uzbekistan has used foreign investment to improve transport connectivity within the country by developing railways and roads (very few of its rivers are suitable for navigation). Its transport infrastructure benefited from major improvements with the construction and launch in 2016 of Angren–Pap electrified railway line and the Kamchik Tunnel, which links the Fergana Valley with the rest of Uzbekistan.

## The Continental Factor: Conclusions for EEU Countries

For centuries, Eurasia’s economic development has been all about overcoming distances and moving from the depths of the continent towards maritime transport corridors. It was maritime access that unified Kievan Rus’, the medieval state that controlled the trade route from the Varangians to the Greeks, that linked the Baltic region, the inland regions of Ancient Russia and the Black Sea region. There was also

<sup>28</sup> ‘Report on Economic Potential, Economic Reformation Process, and Measures Taken with the Aim of Further Economic Development of the Republic’, Ministry of Economy of the Republic of Uzbekistan. Available from: <https://mineconomy.uz/ru/node/696>

the Volga trade route that linked the Baltic with the Caspian Sea. The Silk Road led from Eastern Asia, primarily China, to the Mediterranean. Ancient Russia and China made considerable economic gain from being able to access and control these trade routes.<sup>30</sup>

<sup>29</sup> *Transit Transport Issues in Landlocked and Transit Developing Countries. Economic and social commission for Asia and the Pacific. Landlocked Developing Countries Series, No. 1. United Nations, New York, 2003. URL: <http://siteresources.worldbank.org/INTRAN-ETTRADE/Resources/WBI-Training/UN-Landlocked.pdf>*

<sup>30</sup> *The recent accession to the WTO by a number of Eurasian countries can be compared to overcoming trade restrictions and diversifying trade relations. See <http://russ.ru/layout/set/print/pole/Globalizaciya-at-Velikogo-shelkovogo-puti-do-VTO>*



Today, eliminating spatial and interstate barriers and thereby reducing the cost of continental isolation and reaching global markets by accessing sea ports is one of the key dividends integration can bring to EEU countries.

Efforts to expand access to global markets call for new continental links, as well as access to the high seas in order

Infrastructure development is a key priority when it comes to generating higher added value from transits.

Overcoming challenges related to EEU's continental nature would be impossible without the state playing an active and, at times, crucial role in infrastructure development, removing trade barriers, setting technical regulations, as well as conducting trade and economic policy.

The advantages of the continental geography can be best exploited by following a number of macroeconomic 'rules.' A stable environment is a prerequisite for attracting investment needed to sustain proactive efforts aimed at reclaiming the continental space through infrastructure development. For this reason, a system of economic rules, both monetary and budgetary, should be put in place for opening long-term planning horizons and financing long-term investment projects.

The experience of both Western and Eastern economies could be used in addressing the distance factor by combining the European stabilization instruments with the Asian industrial policy model.

The Western experience could serve as a model of fiscal and monetary policy, including prioritizing low inflation and setting thresholds for non-oil and gas budget deficits and controlling public debt.

The Eastern model could serve as a source of inspiration not so much in terms of import substitution policies driven by

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to diversify trade flows. EEU countries could use ports in Russia's Far East to this effect,

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as well as logistics chains of China's Silk Road initiative to enable landlocked countries to access East Asian countries. At the same time, the development of the transit potential between Asia and Europe is also associated with a number of risks, calling for environmental protection and standardization.

cheap national currency,<sup>31</sup> but rather in terms of export promotion. South Korea could serve

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### The experience of both Western and Eastern economies could be used in addressing the distance factor

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as an example of the Asian model of industrial policy, specifically, its way of setting timing requirements and an objective to achieve a specific share on export markets as a condition for receiving government support. These two components could be placed at the core of the Eurasian model of economic growth.

Developing the oil and gas sector is essential for overcoming continental isolation. In terms of competitiveness, the availability of vast energy resources could offset, at least to some extent, the high transport costs of delivering goods to the main export markets. For example, Russian metals and chemical producers benefit from low energy costs.

At the same time, the fact that energy exports account for an important share of national income means dependence on the key export and transit countries. In addition, the abundance of natural resources could undermine the commitment to diversify the economy and develop infrastructure as a way to compensate for the remote location.

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<sup>31</sup> This combination is closer to the Latin American model. While essential for a number of strategic sectors, import substitution cannot serve as a long-term driver of economic growth and technology upgrades.

In itself, the need to rely on transit countries in fuel and energy exports is a restriction related to the continental economy of countries like Russia. In fact, its transit-related conflicts with Ukraine resulted in substantial losses for both sides,<sup>32</sup> forcing Russia to build Europe-bound pipelines bypassing Ukraine. Building submarine pipelines like Nord Stream is one way of dealing with this issue without completely resolving it.

Taking into account the importance of the distance factor for Eurasian countries and the need for large-scale infrastructure projects to overcome these distances, the Eurasian economic model could focus on a number of key priorities:

- *transport sector (developing logistics and transport chains with a focus on high technology and services for added value);*
- *information technology and other services (sectors that do not depend on transport costs and transcending the continental gravity of vast spaces);*
- *economic sectors with low transport costs and high competitiveness in terms of energy and labor costs;*
- *agriculture and food production (benefiting from abundant agricultural land).*

Continental countries should not simply copy solutions used by more advanced coastal

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<sup>32</sup> More often than not, these issues are not factored into the costs related to continental isolation when dealing with energy exports.

countries. Instead, they should be aware of their unique geography and region, economic structure and foreign trade patterns.

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### Engaging in regional coordination and integration is key to reducing transport costs for continental countries

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A number of methods can also prove useful in overcoming continental isolation, including developing transport infrastructure and high technology in logistics, increasing the share of high value-added goods and services in exports so as to minimize transport costs, as well as streamlining transit, border crossings, customs clearance, etc.

Engaging in regional coordination and integration is key to reducing transport costs for continental countries. It would be hard or even impossible for a single country to overcome many of the abovementioned challenges related to remoteness from the coast. The only way of resolving many issues is to tackle them on a regional or macro-regional level by coordinating transport and macroeconomic policies, combining efforts in infrastructure development to facilitate intra-regional trade and reduce the cost of reaching export markets. Regional integration has the potential to strengthen the bargaining position of an integration body with third countries or trade blocks.



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