UKRAINE
NO WAR TODAY, AND PROBABLY NONE IN FUTURE

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The share of FX-linked deposits in total deposits placed with Turkish banks had leapt to a record high of 62.2% as of December 3, central bank data showed on December 9.

The record resulted from the lira crisis that has seen Turkey’s currency collapse in value. FX-linked deposits declined by $1bn w/w to $231bn in the week ending December 3 – but the severe lira depreciation fuelled their lira-denominated value.

The previous record level of such deposits was registered as far back as October 2001 at 61.5% – the year of 2001 brought the greatest economic crisis experienced by Turkey in recent history.

Indicators on the current economic turmoil are exceeding the historic financial tumult suffered in 2001. They are now comparable with what was seen at the end of the 1970s, when a several-years-long great depression in Turkey ended with the military coup in 1980 that led to rule by a junta for three years.

Also on December 9, central bank data showed that foreign investors’ lira swap stock with Turkish banks fell further by $2bn w/w to $2.9bn.

The figure was recorded at $24bn as of March 19, prior to the dismissal of the previous central bank governor by presidential decree.

It should be noted that the figure stood at more than $60bn in 2018.

Remaining foreign capital flows via the equity and lira bond markets are by now at negligible levels.

As of December 3, the central bank’s gross reserves declined to $124.1bn from $126.4bn a week previously, while the net reserves dropped to $22.5bn from $24.7bn.

When the central bank’s $60.4bn of off-balance sheet swap stock is excluded, the net reserves sink to minus $37.9bn as of December 3 from minus $36.2bn a week previously.

“When the central bank’s $60.4bn of off-balance sheet swap stock is excluded, the net reserves sink to minus $37.9bn”
Kosovo faces worst energy crisis in a decade

Valentina Dimitrievska in Skopje

Kosovans will experience 60 days of planned daily power cuts after the government decided on December 24 to implement emergency measures to deal with the energy crisis.

The government said that due to the significant increase in electricity consumption, insufficient domestic power generation and the global energy crisis that has resulted in the enormous increase in electricity prices on international market, the Kosovan energy system is facing huge difficulties.

Difficulties in the electricity supply occurred especially during December 2021 due to breakdowns in the Kosova B power plant’s units and a significant increase in electricity consumption.

"In order to maintain the integrity of the system, the government is announcing emergency measures in the energy supply for a maximum duration of up to sixty days," the government said in the statement.

KEDS said on December 24 said it introduced systematic, temporary electricity outages of two hours due to the deepening energy crisis, the overloads of the electricity system, the increase of consumption due to increased heating and huge difference between consumption and production.

KEDS said that rotating power outage would initially be implemented for 24 hours and that different regions would be cut for two hours at a time.

The distribution company also urged citizens to be careful with their energy consumption and use alternative heating measures.

Customers are being notified of the planned restrictions through the eKesco app.

Kosovo relies heavily on electricity generation from TPPs, but often faces energy crises due to its outdated TPPs. Kosovo is estimated to have the world’s fifth largest reserves of lignite or brown coal of 12bn-14bn tonnes. It produces 95% of electricity from coal, making it the second in the world.

Outdated stations contribute to low domestic production and a global energy crisis has increased import prices.

Meanwhile, Kosovo’s government allocated €20mn to import electricity, which according to Prime Minister Albin Kurti is up to seven times higher than during the same period last year when the price of one MW/h stood at around €60.

Kurti said earlier in December that such energy prices may continue indefinitely and is important to try to save electricity as far as possible.

He promised that the government will address all energy issues within its mandate and that the strategy that will be presented within the first half of 2022 would be the first step in this direction.

Romania to postpone euro adoption target until 2029

Iulian Ernst in Bucharest

The next report on Romania’s euro adoption will set 2029 as the target date, said first deputy governor of the National Bank of Romania (BNR) Florin Georgescu.

"The lack of political will of the decision-makers in the governments that ruled after Romania joined the EU in 2007, is demonstrated by the fact that Romania has changed so far, based on reports prepared by state institutions and experts the target year for the adoption of the euro," explained Georgescu.

The estimate takes into account the current situation of the main macro indicators in the country, which require substantial corrections and time to achieve them.

"The euro adoption calendar is revised typically on an annual basis and is included in the Convergence Report submitted by the government to the European Commission. Initially, Romania set 2014 as the target for euro adoption, but the deadline was repeatedly revised to 2019, 2024 and now 2029.

Romania had a window of opportunity between 2015 and 2017 when it could have applied for the entry into the eurozone’s preparatory mechanism ERM II given that at
Bulgaria is also aiming for euro adoption, though little progress has been made this year, which has been marked by months of political uncertainty amid the repeated failure to form a new government.

“[A]fter Croatia and Bulgaria, it is likely to remain quiet on the euro enlargement front for a very long time. From the perspective of the remaining current potential euro candidates – Czechia, Hungary, Poland and Romania – economic arguments, albeit from different angles, for accession are not convincing at present,” wrote Raiffeisen economists in a comment for bne IntelliNews earlier the year.

that time it met all the nominal convergence criteria set by the Maastricht Treaty (on price stability, the sustainability of public finances and the indebtedness, the stability of the exchange rate and the level of long-term interest rates). At this moment, however, Romania no longer meets all these criteria.

Romania’s repeated delays to its euro adoption process is in contrast to fellow Southeast European EU member Croatia. Despite having only joined the EU in 2013, Croatia is now progressing rapidly towards euro adoption, and the government currently hopes it will join the Eurozone at the beginning of 2023.

Serbian media tycoon takes over Southampton football club

Eldar Dizdarevic in Sarajevo

English football club Southampton has changed hands, as Serbian media tycoon Dragan Solak's Sport Republic completed the acquisition of a controlling stake in the club on January 4, both parties have confirmed.

Southampton didn't share financial details of the deal but according to reports in the British media, Solak, founder and president of the European telecommunications and media company United Group, bought an 80% stake in Southampton for £100mn (€120mn).

Sport Republic acquired the stake from Chinese real estate magnate Gao Jisheng, who has controlled the club since 2017.

Katharina Liebherr, who inherited a stake in the club from her billionaire father Markus Liebherr, will hold onto her 20% stake.

The statement from Southampton said the club had been searching for “the right partner” to take the club forward for two years, after Gao started looking to exit his investment.

“Today we welcome a new beginning with a new ownership group. We have found partners with ambition for the future, but with a clear understanding of what Southampton stands for and the direction we must go in now. The strategy is to push forward with the plans we have had in place over the last two years, but with their support we can now do this with a renewed focus and speed. Continuity, stability, and clarity of the way forward are equally as important as the new initiatives and ideas we can now bring to the club,” the statement said.

Solak is a Serbian media tycoon, who first entered business in 1990, set up motion picture production and distribution company VANS. He began building his business empire in 1992 when he moved from Belgrade first to Ljubljana and then to Prague. He founded Serbia Broadband (SBB) which later grew into United Group.

He helped the Serbian opposition overthrow Slobodan Milosevic in 2000. In Serbia, he is linked to opposition leader Dragan Djilas, although Solak claims that while they are friends they have never done business together. That is why almost every day some of the pro-regime tabloids, close to President Aleksandar Vucic, mention Solak in a negative context in their articles.

United Group, which has been majority owned by private investment firm BC Partners since March 2019, holds media rights to show the Premier League in much of the Balkans, including Serbia, this season.

However, state rival Telekom Srbija is due to take over the rights from the 2022/23 season in a six-season contract. In Serbia, business clashes between United Group and state-owned Telekom Srbija have escalated into what analysts call Serbia’s first cable war.

www.bne.eu
Solak is also the lead investor behind Sport Republic, a London-based investment firm in the sports and entertainment industry though which Southampton Football Club was acquired. Founded by technology, media and telecoms investor Henrik Kraft and football executive Rasmus Ankersen, the firm says its aim is “to apply proprietary intelligence and data analytics to help sports businesses and sports technology companies reach their full potential”.

“My partners and I have experience in long-term investments in the sports and entertainment industry and Sport Republic has been founded to combine this expertise and deliver something unique to the market,” Solak was quoted as saying in a press release published by Southampton Football Club and Sport Republic.

“Southampton has so many of the qualities we have been looking for in a major sports organisation. It has a great management team, excellent talent development, talented teams playing attractive football and a dedicated fan base. We are delighted to be able to complete this acquisition as a first step towards execution of our investment strategy. Southampton will be a cornerstone of the organisation we plan to build.”

Kraft added that “Whilst Southampton is Sport Republic’s first acquisition, we expect more investments to follow over the coming years. Our ambition is to build a portfolio of high influence stakes in football clubs and other sporting assets across the world.”

He added that Sport Republic will also invest in early stage sports technology companies and use its portfolio to accelerate their development. ●

Corruption probe launched at Bosnia's biggest pharmaceuticals manufacturer

Eldar Dizdarevic in Sarajevo

Members of the State Investigation and Protection Agency (SIPA) of Bosnia & Herzegovina searched the premises of Bosnalijek in Sarajevo, the country’s largest pharmaceutical manufacturer, on December 6 and arrested two people.

The Prosecutor's Office of Bosnia & Herzegovina confirmed that SIPA is conducting searches at Bosnalijek due to suspicions of organised and economic crime and corruption.

The prosecution also stated that searches in progress in several cities in Bosnia, and that arrests of other suspects are underway. They said this is an investigation into “multimillion-dollar acts of corruption”.

SIPA representatives also searched the house of Bosnalijek director Nedim Uzunovic, who was questioned during the day.

According to unofficial sources, the prosecution's investigation is focused on the controversial privatisation of Bosnalijek with Russian capital through offshore companies in several countries.

The key country in the disputed transactions was the Czech Republic, where the company Close Ville was founded five years ago. Close Ville reportedly collected Bosnalijek’s claims from Russia and retained a 10% commission.

"Regarding the investigative actions carried out in the company Bosnalijek, we hereby emphasise that we are fully at the disposal of all investigative and control bodies in Bosnia & Herzegovina," Bosnalijek said in a statement.

On several occasions in recent years, all the required documentation has been submitted and full cooperation with all investigative and control bodies has been ensured, the company added added.

“Bonalijek is the largest domestic drug manufacturer and one of the regional leaders in the industry, operating successfully on three continents, exporting to more than 20 countries and employing more than 800 workers. In the last two years, marked by the COVID-19 pandemic, we are fully focused on meeting the needs of the domestic market and we will do our best to confirm and preserve our strategic role for Bosnia & Herzegovina and all our citizens in the coming period. We assure citizens and all our business partners operation and maintenance of all business processes,” the company added. ●
Russia reports poor harvest, Ukraine bumper crop in 2021

Droughts, death of winter crops and a shortage of migrant workers for seasonal field work hit Russia’s 2021 harvests, which was down to a three-year low, the Russian Ministry of Agriculture reports. By contrast, Ukraine had one of its best harvest ever.

Russia and Ukraine are vying with each other for the title of “world’s biggest grain exporter” and agriculture has become a major money spinner for both countries.

Russian farmers had taken in 120.7mn tonnes of grain at the end of 2021, which was 9.6% more than in 2020, according to RosStat statistics. But the grain harvest was at a 3-year low, less by almost 15mn tonnes from the previous year.

The wheat harvest fell too, by 12%, or 10mn tonnes, and amounted to 75.9mn tonnes, off from the Ministry of Agriculture’s start-of-season forecast of 81mn. The barley harvest fell by 14% to 18mn tonnes but the corn harvest was up by 6% more than a year earlier at 14.6mn tonnes.

“The decrease in the volume of cereals was due to the death of winter crops due to drought in many regions of the country,” analysts told the finanz.ru website.

The US Department of Agriculture predicted a Russian harvest of 85mn tonnes of wheat in Russia, but in August sharply lowered the estimate to 72.5mn tonnes due to bad weather hitting some large producing regions including Tatarstan, Bashkortostan and Orenburg. The yield of harvested wheat in the Central Federal District fell by 24% year on year and in the Volga Federal District by as much as 45%.

Falling crop harvests were experienced in 2021 by most of the largest exporting countries, including Canada, Brazil and the United States, where, according to the Ministry of Agriculture, wheat harvest were at their lowest levels in the past 19 years.

A supply gap, coupled with rising demand and record purchases by China for the state food reserve, pushed the average price of wheat on world markets up 31% y/y, according to an estimate by FAO (the Food and Agriculture Organization of the United Nations).
According to Leshchenko, the harvest exceeded the ministry’s preliminary forecast, estimated at 100mn tonnes for the year.

The successful harvest was also due to this year’s state loans to farmers, accounting for $1.1bn in total to boost the industry. Ukrainians started buying and selling land after the 20-year moratorium on land transactions was officially lifted on July 1, 2021.

With 42mn hectares of farmland covering 70% of the country and about 25% of the world’s reserves of black soil, agriculture is Ukraine’s largest export industry.

Officially, large agro-corporations operate on 6mn hectares; small and medium agro-companies on some 11mn hectares.

The harvest alone will add 0.8% to the country’s gross domestic product (GDP), according to the National Bank’s report released in October 2021. In 2020, Ukraine’s agriculture sector generated roughly 9% of its GDP.

Ukraine exported 17% more agricultural products between January and September 2021 than in the same period of 2020.

The country exported roughly $18bn worth of agricultural products, up by $2.6bn compared to 2020, according to the State Statistic Service of Ukraine.

China was the largest importer of Ukrainian agricultural goods this year, accounting for roughly $3bn of exports, a 36% increase compared to 2020. India imported $1.35bn worth of agricultural goods, followed by the Netherlands with $1.2bn.

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**Inflows into EM and Russian securities resume after Christmas sell-off**

Wojciech Kosc in Warsaw

Fund flows reversed and began flowing back into Russia’s securities following a sharp sell-off in the last two months of 2021 on the back of rapidly rising geopolitical tensions.

Fund flow tracker EPFR Global reported that Russian assets saw a net inflow of c$80mn in the week ending on January 6, ending the outflows of the last two months.

Russia’s dollar-denominated Russia Trading System (RTS) index peaked at 1920 in October, but then fell heavily, giving up almost half of all the gains it made over the course of 2021.

The RTS has lain moribund since the 2014 sanctions were imposed following Russia’s annexation of Crimea and the oil price shock of that year, trapped in a trading band of between 900 and 1300. It broke out in 2018 as individual names began to recover. By 2019 there was a broad-based rally that began to lift the index as a whole. The rally was put on hold during 2020 following yet another oil price shock and the start of the coronavirus (COVID-19) pandemic, but resumed in the third quarter once the vaccines appeared.

Russia was one of the world’s best performing markets in 2021 with the RTS up by a third, until the end of October when the US started reporting on a build-up of Russian forces on Ukraine’s border and Russian President Vladimir Putin demanded talks with the US and Nato on a new security deal, backed by the threat of “military and technical” action by Russia if his demands were not met. That lead to a sharp sell-off that saw the RTS index fall to just under 1600 by the end of the year.

US President Joe Biden has conceded starting talks with the Kremlin, which will commence next week on January 10 and go on for four days, as they also include sessions with the leading EU countries and the top military brass at Nato.

Prospects for a deal remain mixed, but there is some common ground, as both Biden and Putin want to restart some of the Cold War-era missile treaties. However, Putin’s insistence on legal guarantees of no further expansion of the Nato alliance will be a major sticking point.

Aside from the tense politics, Russia’s economy looks strong and companies have been earning record profits in 2021 that they are sharing with investors, with record dividend payments that will continue in 2022. Based on the economics, analysts marked Russia up to a Buy at the end of 2021 with an end of target of 2000 for the RTS – provided there are inflows into EM and Russian securities resume after Christmas sell-off.
Elsewhere, the fund flow picture was mostly positive, with China funds reporting net inflows of $2.3bn, the dominant force. In general, Russian flows do well when China does badly, and vice versa.

“During the slow times of early 2022, global investors appear more positive on EM stocks, which should support the Russian stock market in the coming weeks,” Smolyaninov adds. “The Kazakhstan riots are [a] true regional black swan and a point to watch for investment community in the near term, with admittedly very low visibility in terms of investment implications. Yet we doubt they would lead to major outflows from EMEA, Eastern Europe or Russia equity funds unless seriously escalating.”

EM Bonds also had their best week since early September. Global EM bonds funds finally reported net inflows of $475mn, the most significant intake since early September, reports EPFR.

Net flows for the Russian bond funds were muted, as the country is on long New Year and Christmas holidays. While EM bond spreads have seriously narrowed in the past couple of weeks, the pressure from the UST yield curve remains, BCS GM reports.

“Both GEM equity and bond funds suggest renewed global investor interest in the asset class at the beginning of the year, which is positive. Russia-dedicated flows are suppressed by the low season, while Kazakhstan developments have limited impact on regional fund flows so far,” Smolyaninov said.
Yara has “sought positive change by leveraging its presence in Belarus to promote occupational safety and human rights”, the statement said. The sanctions have reduced the company’s ability to “positively influence the safety and well-being of Belaruskali workers”.

According to Yara’s own estimates, the company buys between 10-15% of Belaruskali’s output.

In a previous statement, BITU president Maksim Pazniakou has praised Yara’s efforts to improve worker’s safety at Belaruskali and said that they had asked Yara to continue with this support as long as possible. In an email to the Swedish Confederation of Professional Employees (TCO) last year, BITU international secretary Lizaveta Merlyak said that sanctions against Belaruskali would hurt its workers the most. Merlyak argued that if western companies terminated their contracts with Belarusian state companies, it would bring about a cutback in investments for occupational safety. Furthermore, Merlyak supposed that international sanctions against Belaruskali would allow Russian potash companies to buy Belarusian mines on the cheap.

Since the protests in 2020, many workers have been fired by Belaruskali’s management and several members of BITU have been detained by Belarusian law enforcement agencies for supporting the protests. This sparked an outcry from international human and worker’s rights organisations.

Yara has “sought positive change by leveraging its presence in Belarus to promote occupational safety and human rights”, the statement said. The programme is run in close co-operation with the independent trade union Belarus Independent Trade Union (BITU) as well as in full compliance with applicable sanctions according to the president & CEO of Yara, Svein Tore Holsether.

In the spring of 2021, Yara was one of many companies to come under fire from the exiled Belarusian opposition for its co-operation with Belaruskali, demanding that Yara discontinue its co-operation. Belaruskali is one of the world’s largest potash producers and exports its products all around the globe. It was included in the sanctions imposed after the Lukashenko regime forced a commercial Ryanair flight to land in Minsk and arrested top opposition blogger Roman Protasevich and his girlfriend on May 23 last year.

But of course circumstances and market conditions are different this time around. Today, most of the business is (re-)financed locally and not built on imported capital. All major (Western) banking players in the region are running loan-to-deposit ratios in the range of 70-80%.

In this respect, the current business activities can be considered sustainable from a macro-financial perspective. There is no credit growth that leads to macroeconomic imbalances. And especially in markets like Russia, increasingly local (re)financing has become more and more important for major international banks for other reasons as well.

Banks support V-shaped recovery

This time there was no deleveraging during the crisis. Banks contributed to the V-shaped economic recovery. The latter has then led to low NPLs and low risk costs. Moreover, the rapid economic recovery has had an inflationary effect, leading to key interest rate hikes.

Once a year, we at Raiffeisen Research take a close look at regional banking trends in our CEE Banking Report. And before what we hope will be a quiet and peaceful Christmas and New Year, here is a big overview of the most burning CEE banking sector issues.

To give the most important message right away: Leading Western CEE banks have made their contribution to overcoming the crisis. This can be seen in the almost double-digit credit growth rates of exposures to the CE/SEE region in the last 12-18 months.

We at Raiffeisen Research have been monitoring the business of Western banks in CEE – including our valued competitors – for decades. And we have only seen such balance sheet expansions as in the last 12-24 months – if then – in the so-called “CEE bonanza phase” i.e. in the run-up to the Global Financial Crisis and the following CEE banking confidence crisis.

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The Polish banking sector continues to be weighed down by the FX mortgage issue. The FSA's proposal from late 2020 has not been implemented sector-wide as banks attempt to approach their own settlement programmes based on a cost-sharing principle with borrowers (most prominent here are Bank Millennium and mBank). Still court cases continue to rise (+84% ytd) as the first-instance rulings tend to side with the debtors rather than banks. During the first nine months of 2021 banks set aside more than PLN3.7bn (€806mn) of legal risk provisions for current and expected future litigation outcomes.

As good as it gets, more limited upside from here
Outside Poland, all sounds like a perfect alignment of many supportive trends and in principle we expect a solid development in the CEE banking industry also for 2022. Nevertheless, the 2021 trends cannot be extrapolated and the more we move into the post-crisis phase, the more regulatory and “normal” market/country drivers will be once again interesting to watch.

On the one hand we see the risk that there will be another dose of ‘extra’ banking taxation, with Slovakia being the prime example. We would also expect that regulators will return to the idea of capping too much loan expansion, as credit cycles in certain countries and/or market segments were already pretty mature pre-crisis. A step-up in the counter-cyclical capital buffer (CCyB) is planned in the Czech Republic (up to 2%), Bulgaria (1%) and Romania (0.5%) and the reinstatement of bank-specific O-SII buffers has been approved in Hungary.

On the flip side of the rate-hiking cycles, capital will also be hit by a negative revaluation of banks’ portfolios of debt securities amid the corresponding spike in sovereign bond yields. The actual mark-to-market loss booked in the comprehensive P&L would of course depend on the amount of bonds accounted for at fair value as well as the portfolio’s currency mix and average duration, but we generally note larger holdings of government bonds by banks in Albania, Romania, Ukraine, Hungary, Poland and Serbia.

In the case of Russia, slowing economic growth will test the sector’s unresolved credit risks, and a steep rise in interest rates heralds a moderation in lending. Hence the stellar results in terms of profitability might not be repeated in 2022. In 2021 the Russian banking sector is likely to achieve the highest profitability seen since 2007/2008.

Overall, most key CEE banking players have still not issued very tangible guidance for 2022 due to ongoing uncertainties around a mix of the pandemic, interest rate and CPI effects, supply chain disruptions and the like. Nevertheless, the upcoming year(s) should give reason for hope, as the monetary tightening cycle should provide a shield against reasonably normalising risk costs and inflationary pressure on operating costs. The main downsides come from volatile foreign currencies, regulatory interventions and the elephant in the room, i.e. geopolitical tensions. We will come to this risk factor later.
More and more ‘local’ champions

Apart from the overall market trends, it is also always good to know how market share trends that reflect the individual positioning of major banking groups on a country level are shaping CEE banking markets. Here we observe the following three interesting trends. First, more and more ‘local’ champions are emerging in individual banking markets in Central and Southeastern Europe. A good example is Banca Transilvania in Romania. The planned merger of PPF and Moneta Money Bank would also create a sizeable local champion that can compete with the three largest foreign-owned banks in Czechia. Sometimes politics also plays a role here. The Hungarian Bank Holding (a merger of MKB, Takarek and Budapest Bank) is set to become a large Central European bank in terms of total assets (with a 4% market share in the CE-3 asset base and 15% on the Hungarian market).

Secondly, more and more cross-border regional champions are emerging out of CEE. Hungarian OTP is THE winner in terms of upscaling in recent years. Based on solid M&A activity, the CEE asset base of OTP has passed the €60bn threshold and is now larger than the one of Intesa and ING, and is chasing the fourth-largest CEE bank (SoCGen). The second regional champion NLB now has a regional asset base above €20bn. But so far there have been no cannibalisation of the Western European players in the region.

And this brings us to another important trend. All Western European banking or banking groups active in the region are strategically more inclined towards the region. The aggregate market shares of the leading banks have remained more or less constant in recent years. The three large pan-European CEE banks (Erste, RBI, UniCredit) continue to have market shares of close to 20% in Central Europe and 30% in SEE, while the leading 5-6 foreign banks continue to hold market shares of 30%+ in Central Europe and 45% in SEE. Recent balance sheet data also show that the two largest lenders in CEE are (once again) two Austrian pan-European lenders – Erste and RBI, the latter once again slightly ahead of the friendly competitor UniCredit. RBI and Erste are the only lenders with an asset base above €100bn in CEE.

M&A activity in CE/SEE vs divestment and/or organic market trends in Eastern Europe & Russia

The leading Western CEE banks are currently participating very actively in the consolidation process, which is regaining full momentum. Since the last edition of our CEE Banking Sector Report, we have witnessed remarkably stronger M&A activity and the return of the former main players to the scene, with more than €34bn of assets subject of either concluded or signed agreements in the region. The chief motive is operational upscaling as the best medicine against unabated competitive pressure.

On this front the recent headlines were made by RBI (acquisitions in Serbia and Czechia, divestment in Bulgaria), Erste (upscaling in Hungary), KBC (acquisitions in Slovakia and Bulgaria), Sberbank (divestment in Bosnia, Croatia, Hungary and Serbia) and OTP (divestment in Slovakia, acquisitions in Slovenia, Uzbekistan and Albania).

Interestingly, a certain stability of market shares – albeit at very different levels – also applies to the Eastern Europe region. Here the market share of the three banks operating in Russia (and also in the region) has remained constant at 3.8% since 2013/2014. This constant figure conceals slight shifts. Currently, RBI is the leading Western CEE bank with the most prominent presence in the region. It has a market share of 1.6% compared with 1.3% in 2013/2014. UniCredit's regional market share has decreased from 1.4% to 1.0% in the same period, while Societe Generale's market share has risen slightly from 1.1% to 1.2%.

These key figures naturally reflect above all the dynamics in the Russian market. Here, Raiffeisenbank is now slightly ahead of Societe Generale and UniCredit (1.2% and 1.0% respectively) with a market share of 1.3%. In 2013/2014, the competitors from France and Italy were larger than RBI's Russian subsidiary (market shares were then 1.6% UniCredit, 1.5% SocGen vs. 1.2% Raiffeisen).

Overall, the largest universal foreign lenders (RBI, UniCredit, SocGen) stay well entrenched in their niche on the Russian market, though somewhat behind the market average in retail loan growth and profitability (except for RBI) in 2021. With the departure of Citi from the Russian retail lending market (its local retail business represented <10% of total assets) the market share of the remaining entity will fall below 1%.

(Geo-)politics matter in EE but no deleveraging

We have already emphasised the positive business and volume development in the CE/SEE banking sectors. Consolidated cross-border claims of Western banks towards the CE/SEE region increased in double-digit territory over the last 12-24 months. (+12 % December 2019 to June 2021, +14% June 2020 until June 2021). In contrast, cross-border positions (on a consolidated basis, i.e. including local claims in LCY and FCY plus cross-border businesses) remained more or less flattish in the EE region over the last 12-24 months.
“In total exposure terms the Russian market is only the third-largest country-level exposure of Western banks in the CEE region, well behind Czechia and Poland.”

Measured from December 2019 to June 2021, cross-border exposures to the EE region dropped by 4%; from June 2020 to June 2021 they increased by 8%. However, this flattish development should not be seen as negative either, in the aftermath of the GFC (as well as in the context of the Russia/Ukraine crisis in 2014) there was a brutal (external) deleveraging in EE banking exposures. Therefore stability is also a certain success here. Moreover, everybody still operating in the region is doing so based on very selective and risk-oriented business policies.

Overall, aggregated exposure of Western banks towards the EE region has reached its lowest point in relative terms over the last two decades in 2021. The reference to geopolitics is also reflected in the fact that the relative decline trend accelerated substantially from 2014 to 2016. During this period the share of the EE region in international banking exposures into the CEE region dropped from 22% to 14% (based on substantial nominal cuts in exposures), and is now hovering around 11%. The Russian banking market currently represents some 9% of CEE exposures at Western banks. This sounds still substantial but has to be put into a broader context. Western banks have more or less the same amount of money at work in Slovakia as in Russia, while Slovak GDP represents some 6-7% of Russia’s economic wealth (in euro terms).

Some further modest downside with regard to Western bank positions towards Russia might be looming with the partial exit of Citi from the retail market in Russia. However, we would not over dramatise this development either. In total exposure terms the Russian market still represents the third-largest country-level exposure of Western banks in international banking statistics towards the CEE region, well behind Czechia and Poland, but still somewhat ahead of Slovakia and Romania.

**Back to square one, is Central Europe again the place to be?**

The “winners” in terms of increased importance in cross-border exposures in the CEE region are the Central European countries. We see this trend as a reflection of relative stability: solid growth in Czechia and Slovakia, a revival of attention towards the Hungarian market, while exposures towards Poland are not really moving in either direction recently (up or down). Therefore exposures of international banks towards the CE region in relation to overall CEE exposures are currently standing at their highest level since 2004 (close to 70% of total), while we still remain somewhat below historical peaks in SEE (and obviously well below historical peaks in EE).

At least in the mass business, it looks like the Western banks are returning to where they started their Eastern expansion. In the light of increasing geopolitical risks, this makes sense; from this perspective, Central European EU countries are much more suitable for mass business. Moreover, the regional markets here have retained their relative attractiveness, and we see further euro introductions by the end of this decade (beyond Croatia and Bulgaria), which will maintain market attractiveness.

Given all the trends and figures sketched above, we labelled our CEE Banking Report 2021 “As good as it gets in (post-) crisis times”. This title also reflects the hope that we are finally approaching post-crisis times in the course of 2022.

Gunter Deuber is chief economist of Raiffeisen Bank in Vienna. This article was prepared with Ruslan Gadeev & Jovan Sikimic of Raiffeisen Research in Vienna together with local research teams across CEE.

The CEE Banking Sector Report is a well-established annual flagship study of Raiffeisen Research. Once a year the entire Raiffeisen Research team in CEE and Vienna analyse banking sector dynamics in the CEE region in detail. In addition to country coverage with local flavour, we once again documented market shares, balance sheet totals and financials of the leading (Western) cross-border CEE banks. The same holds true for cross-country trends for market shares, business dynamics, asset quality and profitability. For more information plus data on CEE banking sectors see our 2021 edition of our flagship CEE Banking Sector Report (for registered users at the Raiffeisen Research Portal).
PPF still has the deal-making mojo after death of founder Petr Kellner

Robert Anderson in Prague

PPF, the adventurous Czech investment group founded by the late billionaire Petr Kellner, could be poised to divest one of its last major assets in Russia, a country in which it has been one of the biggest foreign financial players for the past 20 years.

Russian investment giant Sistema is reported to be close to buying PPF's consumer finance unit Home Credit's operations in Russia and Kazakhstan, after earlier speculation that Hungary's OTP Bank was the favoured buyer.

The report of the sale – which neither side has confirmed – comes after speculation over several months that the unit was for sale. These rumours were boosted by PPF commenting last month that the group was looking to sell operations, or partner them with other companies, in markets with "limited potential".

The potential sale of what has been one of PPF’s crown jewels has naturally sparked speculation that CEO Ladislav Bartonícek is having a clearout of assets and is narrowing the group’s focus following the death of Kellner in a helicopter crash in March last year.

PPF insiders confirm that a lot of deals are currently in the pipeline, raising the question of what the group’s investment strategy now is, and what other businesses among the group’s €40bn of assets might be up for grabs.

Deal-making legend
Petr Kellner was a deal-making legend and by far the most famous and successful Czech businessman of his generation.

The richest man in Central Europe, with a personal wealth estimated at $17.5bn by Forbes, he made his fortune in the ‘Wild East’ of the Czech transformation from Communism in the early 1990s, becoming a major regional player in consumer finance, telecoms and media.

He was also one of the first regional tycoons to outgrow the local markets and expand globally. After launching the Home Credit consumer finance format in Central Europe in 1997, he expanded it east to Russia in 2002, and then from 2007 into China, making it the world’s largest non-banking consumer lender.

In Russia, Kellner diversified into real estate, agriculture (Rav Agro), electronics retail (Eldorado) and gold mining (Polymetal), as well as insurance, by swapping stakes – and sometimes going head to head – with the country’s powerful oligarchs.

But even before his death last year PPF was beginning to shift its assets away from Russia and Asia and back into developed European markets – in particular the Czech Republic itself – as well as the Balkans.

PPF has been selling down its Russian assets gradually over the past decade, reducing its stake in Polymetal and disposing of the Eldorado electronics and domestic appliances chain in 2016. But the sale of Home Credit Russia would be a huge step-up in this disposal programme.

Arguably this shift has been accelerated by PPF’s decline in political influence following the death of Kellner, and by the reverses for Czech President Milos Zeman’s foreign policy of pursuing closer links with Beijing and Moscow. Kellner had forged a bond with Zeman, especially over PPF’s drive into China, and the billionaire even gave the president a lift back in a private jet from a trip to China in 2014. This kind of political support and ‘cover’ is just no longer available or possible.

Cutting exposures
There is now speculation that as well as Home Credit Russia, PPF is targeting disposals of Home Credit’s Asian operations in India, Vietnam, Indonesia and the Philippines. Bloomberg has reported that those assets could be worth up to $2.5bn.

In China PPF is reducing its exposure and is rumoured to be looking for a partner. Home Credit operating revenue there fell to €725mn in the first half, from €1.6bn a year ago, under pressure from Beijing’s restrictions on banks’ access to local funding sources.

PPF’s disposals partly reflect Home Credit’s struggle in Russia, China and India with problem loans, which has been
accentuated by the outbreak of the coronavirus (COVID-19) pandemic. PPF made its first ever loss in 2020 of €291mn because of impairments at Home Credit. By refocusing on more developed markets, PPF can diversify its portfolio and stabilise its returns.

PPF CFO Katerina Jiraskova said in November that the pandemic had hit Home Credit hard but that the PPF group’s diversification had enabled it to bounce back to make a net profit of €208mn in the first half of 2021.

“PPF’s first half-year results demonstrate that the group is able to withstand the immediate and lingering effects of the COVID pandemic through the sectoral and geographic diversification of its portfolio. Having recorded profitability for two consecutive half-year periods, PPF is ready to undertake new transactions while investing in its existing assets,” she said.

**Opportunistic investments**

Already as part of its gradual shift back into Europe, PPF has in the past few years bought assets from major European and US companies, becoming a major presence in CEE telecoms through acquisitions from Telefonica and Telenor, bringing with it 18mn customers across Czechia, Slovakia, Bulgaria and Serbia, as well as the purchase of regional TV group CME with a potential 45mn viewers in Czechia, Slovakia, Bulgaria, Romania and Slovenia.

Insiders say new CEO Ladislav Bartonicek, who was with Kellner at PPF since the beginning, has continued in the direction set by the tycoon of focusing on more mature markets whilst also keeping an eye on opportunistic deals.

Since Kellner’s death the acquisition and investment drive has continued unabated, notably with the acquisition by reverse takeover of the Czech lender Moneta Money Bank. By combining Moneta with PPF’s digital bank Air Bank, Kellner’s dream of building a major Czech-owned bank has finally been fulfilled. The combined banking group will have a total of 2.5mn customers in a country of 10.7mn people, putting it in third place in terms of customers, and ranking it second in consumer finance.

At the same time, the group has continued to make opportunistic investments outside its favoured finance, telecoms and media sectors, in segments where it sees the chance to pick up assets cheaply and consolidate a fragmented market.

It created a sailboat charter joint venture with France’s Groupe Beneteau to consolidate the fragmented charter boat market. It has become the biggest player in a sector struggling because of COVID-19, but one potentially with bright prospects as rising wealth allows middle-class clients to use sailboat charters as a kind of nautical Airbnb.

PPF has also made a contrarian bet on the revival of the office real estate market, making a deal in Florida worth around $315mn and another in Georgia worth more than $100mn, and entering the Polish market with the acquisition of the New City business park in Warsaw last month.

As part of the disposal of its stake in Czech retail internet site Mall.cz, PPF has also built a consumer electronics merchant Fast CR, with its Planeo Elektro retail chain and its own brand Sencor, in which it has a 40% shareholding.

At the same time, PPF has been investing significantly in its own businesses, putting €280mn into its biotech arm Sotio, hiring top Western European talent for engineering company Škoda B.V. (not related to the carmaker), and investing CZK27bn (€1.11bn) since 2015 into regional telecom infrastructure unit Cetin’s network.

PPF is also building up regional TV group CME’s Voyo streaming service by acquiring and commissioning new content. The relaunched Voyo service will now offer a locally customised regional streaming platform of films and TV shows.

To reduce leverage, PPF has also made several disposals in the telecoms sector. It sold a 30% stake in Cetin to Singapore’s state investment fund GIC, in a deal estimated to be worth around €2.5bn. It has also recently sold Telenor Montenegro, which was deemed too small to offer significant growth potential.

**What would Kellner do?**

Bartonicek, in a recent interview with Czech Forbes, admitted that he still sometimes asked himself what Kellner would do, and that he was more cautious than the famous dealmaker.

“He was a bigger risk taker, that’s for sure. It has to do with the fact that when you are an absolute majority owner, your decision-making works a little differently. It depends on you. I’m partly responsible for my assets, but primarily for his family’s assets, so it’s different,” he told Forbes.

However, the spate of deals certainly demonstrates that PPF has not lost its mojo since the death of Kellner and its switch into developed markets.

Nevertheless, there is still speculation over the long-term future of the group, given that it is now 99% owned by Kellner’s widow, Renata Kellnerova, with Bartonicek running the operations of what is now almost a glorified family office.

Kellnerova – who inherited a fortune worth €14.7bn, according to Forbes – maintains an even lower profile than her late husband did, and little is known about how much oversight she exercises in the business. Wouldn’t she be more prepared to accept offers to sell out than if her husband were still leading the group?

With her showjumper daughter Anna regularly linked with Czech energy baron Daniel Kretinsky, there are also persistent rumours that the country’s most high-profile tycoon could soon exercise influence over PPF’s business strategy, after having often been a junior partner in Kellner’s corporate raiding in the past. ●

www.bne.eu
The buyer of Rolf is the car dealer KlychAvto, was started in the southern Krasnodar region in 2001 by Viktor Sergeev as an exclusive Mercredes dealership and quickly become one of the largest players on the market (fifth-largest with revenues of RUB110bn ($1.49bn) in 2020 versus Rolf’s leading RUB258bn).

KlychAvto has actively expanded in other regions, in 2020 alone acquiring one of the largest Siberian dealers Eurasia Motors and St Petersburg assets of Inchcape dealer, The Bell reminds.

Petrov commented to Forbes that after the sale a "very attractive company" will be formed with a turnover of close to RUB500bn and an initial public offering potential (IPO) will be held. To remind, Petrov himself was considering an IPO of Rolf for at least three times the value he got from the sale.

He said that he will reinvest the proceeds in an industry where "one could [freely] do business, rather than fence off absurd accusations".

The Bell reminds that the legal experts saw accusations against Petrov as absurd, with the criminal case based on a simple currency transaction with offshore subsidiaries. The case was linked to corporate raiding and Petrov's political activity as part of Just Russia.

One of Russia’s oldest car dealerships, the company was set up by former taxi driver Petrov in the early 90s. Petrov built the company up from nothing by doing honest business and offering value for money at a time when the car sales and import business was highly corrupt, he told bne IntelliNews in an exclusive interview “Sergei Petrov – Russia's billionaire car salesman”. The company was called Rolf to emphasis its foreignness as Rolf is never used as a name in Russia.

Petrov also set Rolf Leasing, which was successfully spun off and sold to Baring Vostok fund and Delta Leasing in 2004 to become the leading Rusisan leasing player Europlan.

Owner of Russia's largest car dealer Rolf forced to sell

bne IntelliNews

Russia's largest car dealer Rolf, owned by Sergei Petrov has been sold to rival KlychAvto for an undisclosed amount, The Bell wrote citing the announcement of Alfa Bank that will finance the deal. Unnamed sources value the deal at $400mn-$500mn, which is at least three times less than Petrov had initially planned to cash in from selling the company.

Petrov had criminal charges brought against him and the top management of his company in 2019 and since then has been looking to sell up. The story was closely followed by bne IntelliNews as an example of how dangerous it is to be successful in Russia overshadowed by potential criminal charges and corporate raiding.

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bne IntelliNews

Russian retail consolidation continues as Lenta buys e-grocer Utkonos

bne IntelliNews

One of Russia's mid-cap food retailers, Lenta, has announced its intentions to acquire the Utkonos e-grocery service for RUB20bn ($270mn) to expand its online market share and acquire unique competences and loyal customer base.

As followed closely by bne IntelliNews, Russian retail turnover is anticipated to keep growing and to catch up with the pre-coronavirus (COVID-19) levels of 2019. The sector has entered a phase of rapid consolidation and mergers and acquisitions were expected to be the main growth driver for the largest Russian food retailers.
Utkonos is one of the top 10 e-grocery operators in Russia, which is the fastest-growing foodtech and e-grocery segment.

The Lenta/Utkonos deal will be financed by Severgroup that will acquire an additional issue of Lenta's shares under a closed subscription. At the end of 2019 Lenta was acquired by Severgroup of steel tycoon Alexei Mordashov, narrowly outbidding Magnit, its retailing peer. Severgroup also holds a stake in Utkonos.

While previously Severgroup did not roll out a comprehensive strategy for Lenta, the company started to aggressively expand through M&As.

"The acquisition of Utkonos will enable Lenta to significantly expand its online market share with an additional delivery platform featuring a loyal customer base, unique competencies and competitive advantages and the ability to compete in the Moscow online market more effectively, especially within the upper-middle and premium segments," the company said in a press release.

Utkonos is an online-only food retailer based in Moscow and is a pioneer of the e-grocery segment in Russia. In 2020, Utkonos’ share of the Moscow e-grocery market amounted to approximately 10%.

In 2020 Utkonos reached 2.7mn orders with an average ticket of RUB5,359. In 1H21, Utkonos total sales grew by 11% compared to the same period of the previous year to RUB7.8bn.

Following the deal completion, the CEO of Utkonos Danny Perekalsky will take the position of the CEO of Online business unit Lenta-U, reporting to CEO of Lenta, Vladimir Sorokin. So far, Lenta did not change its performance guidance for 2021, but will provide 2022 guidance in February 2022.

Lenta posted a 13% year-on-year gain in revenues in 3Q21, with EBITDA up by 31% y/y and a 91% y/y gain in net income. The top line growth was driven by a 3.5% advance in like for like (LfL) sales, as well as by larger sales surface due to acquired 190 supermarkets and 44 convenience stores.

BCS Global Markets sees the results of Lenta in 3Q21 as solid, with strong margins (EBITDA margin up by 119 basis points to 8.8% and net margin up to 3.5%). Previously Lenta showed compressed margins in 2Q21.

Sberbank CIB attributed the "decent" gains of Lenta in the reporting quarter mostly to the recent consolidation of the chains Billa and Semya. The analysts see an 8% EBITDA margin target for 2021 as feasible due to the effects of the M&A.

Two investment funds buy Bulgarian IT company Chaos

bne IntelliNews

A Associates, a global growth private equity firm, and LEA Partners, a technology focused private equity firm, are acquiring Bulgarian IT company Chaos, it said in a press release on January 11.

Subsequently, Chaos, which is specialised in photorealistic rendering technology, will merge with Enscape, a developer of real-time rendering and design workflow technology for the Architecture, Engineering and Construction (AEC) industries.

"The merger will establish a global leader in the 3D visualisation and design workflow software sectors, with a focus on the AEC, Visual Effects (VFX) and Product Design verticals," Chaos said in the press release.

The new company will retain the name Chaos. It will focus on developing and strengthening its product portfolio to create a comprehensive end-to-end visualisation ecosystem.

Founded in 1997, Chaos has offices in Sofia, Prague, Seoul, Tokyo, and Los Angeles.
Otkritie bank nearly went bust in 2017 as part of the so-called Garden Ring bank crisis. It was eventually taken over by the Central Bank of Russia (CBR), which has put the bank back on its feet. Today it is the sixth-largest banking group in Russia by total assets and one of the top three fastest growing financial institutions in the country. The rescue is complete.

A comprehensive overhaul of the bank’s business and model resulted in Otkritie’s assets rising by an average rate of 22% in the last three years, twice as fast as its larger state-owned rivals, and made it one of the top three fastest growing financial institutions in Russia. And in the first nine months of this year it posted a 1.9-fold year-on-year jump in net profit to RUB58.7bn ($0.8bn), with the return on tangible equity (ROTE) up at 19.1% from 10.9% for the same period a year earlier.

Russia’s banks have been booming and Otkritie back on its feet. Wholly owned by the CBR, it hopes to sell it off or float the first packet to 15-20% of its shares as early as the first half next year, market conditions permitting.

**Near death experience**
The Garden Ring crisis, so named as it affected half a dozen large commercial banks that mostly have their offices inside the Garden Ring road that encircles central Moscow, started with the collapse of Financial Corporate Otkritie and takeover by the CBR at the end of August 2017 after months of speculation and led to a RUB1.1 trillion ($16bn) bailout. It was quickly followed by the takeover of Binbank, another large commercial bank, which got caught in the flak and ran to the regulator on September 20 the same year.

But the antecedents of the mini-meltdown, that at one point looked like it might threaten the stability of Russia’s entire financial system, go back to a new rule introduced that required Russian banks to have the local equivalent of a triple A rating from the domestic Analytical Credit Rating Agency (ACRA) if they wanted to hold the deposits of state-owned enterprises (SOEs). ACRA downgraded Otkritie and several of its peers in April that year. The SOEs had to withdraw their money and that made the other depositors nervous, who began to withdraw their money too and the whole thing threatened to snowball into a classic bank run.

In the following months there was a mad scramble to shore up the bank’s liquidity and several turned to the CBR for help. Loans on the interbank market froze up as rumours of a “black list” circulated and volumes on the repo market soared, where banks can temporarily trade in any bonds they hold for cash. But the valiant efforts by management to rescue the struggling bank came to nought and in order to prevent a systemic meltdown the CBR decided to step at the end of the summer.

Some confusion remains to this day as to what actually happened. Dmitry Mints, whose family was formerly a shareholder in Otkritie and whose O1 real estate company remained a big customer of the bank in 2017, told bne IntelliNews in an exclusive interview that the CBR had acted very aggressively and had to some extent precipitated the crisis.

**Financial rehab**
At the start of 2017 the CBR had already set up the Banking Sector Consolidation Fund (BSCF), a special vehicle that allowed the central bank to be in the unusual position where it is both the banking sector regulator and own banks. The advantage of this setup is there is no need for an expensive bail-out, as the CBR backing should be enough to reassure depositors the bank won’t collapse and put an end to the bank run. The plan from the beginning was to allow Otkritie to recover and then to eventually sell it again.

“The Bank of Russia put Otkritie into the consolidation fund along with several of its other holdings, including Lukoil Garant pension fund, Rosgosstrakh insurance company and RGS Bank, a small car loans specialist,” says Dmitry Levin, the deputy CEO of Otkritie, who was appointed by the CBR after it took over.

The next year the Baltic Leasing company and Life Insurance company were also added. Finally, in 2019 Otkritie was merged with BIN bank on July 2, 2018 and from the next day the combined assets exited the rehabilitation programme and began to function as a regular bank.
“In the first nine months of 2021, the bank doubled net income y/y to RUB58.7bn – the highest in Otkritie’s recent history. At the same time, asset quality remained among the highest on the market.”

In the first nine months of 2021, the bank doubled net income y/y to RUB58.7bn – the highest in Otkritie’s recent history. At the same time, asset quality remained among the highest on the market, with non-performing loans (NPLs) at less than 3% of the total portfolio.

“Today we are a normal bank. At the same time, the CBR had created a so-called “bad bank” on the basis of Trust Bank [which also failed during the crisis] and put all the bad debt from the rehabilitation programme into that,” says Levin. “The CBR also took PromSvyazBank [which also failed] and used that to create a bank that specialises in the defence industry.”

Nevertheless, Otkritie remains directly and 100% owned by the CBR. Three of the central bank’s employees sit on Otkritie board of directors, as well as the Deputy Minister of Finance, but to that the bank has added five independent directors and the CBR maintains Chinese walls between the management of the bank and the department that regulates the banking sector. Mikhail Zadornov, a well-known banker and former Finance Minister, is the CEO and heads the board.

Zadornov is best known for taking over the state-owned behemoth VTB’s retail arm, VTB-24, and building it up into one of Russia’s leading retail banks. Levin also has 30 years of experience and is the former CEO of Russky Standart Bank that pioneered the unsecured retail lending in Russia that caused a revolution in the way Russian banking is done in the noughties.

New business model
The business model was restructured. Previously Otkritie had focused on term deposits, but under the new model Otkritie has been targeting various niche businesses and focusing on becoming a leader in each, sometimes using its subsidiaries to become a leader in a very specific niche.

Levin said one of the first changes was to zero in on both the retail and corporate current accounts business, which provide the main source of funding for the bank’s business. Today 44% of all the bank’s liabilities are current accounts.

Other businesses that Otkritie has made its own are issuing credit cards and payroll programmes for companies, and the bank is especially strong in catering to small and medium-sized enterprises (SMEs).

“We hold a 10% market share of the SME business, together with our subsidiary online bank Tochka,” says Levin. “Our group has about 530,000 accounts that hold half a trillion rubles ($6.8bn). We are also active in escrow accounts. The law was changed for developers collecting pre-paid apartment sales. Developers used to collect the payments and use the money to build the apartments. Now they have to raise financing for developments and the buyers’ money is held in escrow while that is going on, so if the project fails they won’t lose their money. We have about RUB150bn in escrow accounts, which makes us the fourth-biggest player on the real estate development financing market”.

The strategy was updated earlier this year where Otkritie will leverage its digital business model and increase cross sales between units as well as by adding more third-party partners, which can be quickly integrated through its OpenAPI.

Levin says this should help the bank hit its annual net income target of at least RUB100bn by 2023 and become a market leader in terms of return on equity (RoE) of at least 15% by 2023, Zadornov said in September interview.

Otkritie remains a universal bank and Levin says that the business is now mostly evenly divided between retail and corporate banking, while less attention is spent on the term deposits business.

“We changed the model to decrease the speculative rates on term deposits, especially in retail, and pay more attention to retail and corporate accounts. As of 30 September we had total liabilities of around RUB2.2 trillion ($27.1bn).”

The bank funds almost all its business from these liabilities and only issues about RUB30bn-RUB40bn a year on the local bond market, and then mainly to build out a curve with bond investors that is available should management want to increase borrowing using bonds in the future.

“We have a healthy loans-deposit ratio of 89%,” says Levin. “The balance sheet is liquid and the obligations side is also healthy. For the first nine months of this year the net interest rate margin was at a comfortable 4.8%.”

The bank’s capital adequacy ratio (CAR) – the share of cash a bank keeps on call to meet withdrawals – is also healthy at 14.5%, which is well above the mandatory minimum, but not quite the 20% emerging market banks often like to have to deal with economic shocks.

Ratings and privatisation
The bank has returned to fast growth since the problems it had with ratings in 2017, and now they have rapidly improved as a result.

The bank has four sets of ratings in all – two domestic and two international. Otkritie’s ratings from ACRA have been increased seven notches to AA, while the other Russian ratings
agency Expert has increased them three notches. Otkritie is also rated by Moody’s, which has increased its rating three notches to Ba2, and Fitch has upgraded the bank to BB+.

The CBR’s plan from the start has been to sell all the banks it took over in 2017 and with the strong profits Otkritie is now earning that is possible. As bne IntelliNews has reported, Russia has been enjoying an IPO boom in the last 18 months, although after geopolitical tensions reappeared in October the market sold off and the IPO window may be closing now.

“The CBR’s goal has always been to reduce the share of state-owned banks in the system and privatise our bank,” says Levin. “It will be sold either by IPO or to a strategic investor. The CBR has said that both options are acceptable.”

As bne IntelliNews has reported, the pandemic had a very muted effect on the Russian bank sector, which saw profits grow in 2020 and currently are enjoying their most profitable year since Russia’s economy slowed to zero in 2013. The state-owned banking giant Sber (formerly known as Sberbank) earned RUB1.4 trillion in the first nine months of this year by itself, whereas in 2016 the entire sector earned just under RUB1 trillion for the full year. This year the sector should earn about double that.

Levin says there are three things driving the current strong bank sector results. The first is new businesses are flourishing, such as lending and factoring that are adding to bottom lines. The second is the cost of risk is falling and is now low. Banks have invested heavily in their models and data management to further improve the quality of their business and that has been paying off.

Finally, banks have been a big winner from the pandemic in the sense that it was a strong catalyst for the technological transformation that was already under way. Otkritie has invested over $1bn into IT in the last three years and now 95% of its interactions with customers are online and its Tochka bank that specialises in the SME business has no branches at all.

Even the number of branches at Otkritie – and it has traditionally been one of Russia’s strongest retail banks – has been falling from 750 branches in 2018 to 480 as of September 2021 and is expected to further decrease to 400 by the end of 2022, says Levin.

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**Omicron variant ends Romania’s stock market rally**

Iulian Ernst in Bucharest

After continuing to soar through Romania’s recent political crisis, the Bucharest Stock Exchange (BVB) was badly hit by the confirmation of the new variant of COVID-19 virus, omicron. The blue chip BET index suffered the steepest daily decline since mid-2020 on the last trading day of the month, and ended the month marginally (1.1%) lower than it started.

On November 26, the day the World Health Organization (WHO) designated omicron a variant of concern, the BET index fell 3.41%, the steepest daily decline since June 2020, while the BE-NG index of energy and utility companies plunged by 4.12%.

The whole last week of November was impacted by the bad news related to the new COVID-19 developments, which prompted caution among investors.

On a weekly basis, Romania’s stock market indices posted the steepest decline since the COVID-19 shock in February-March last year.

In Romania, the period coincided with the stabilisation of the political situation by the formation of a grand coalition between the National Liberal Party (PNL) and Social Democratic Party (PSD). However, this political arrangement has not generated optimism among investors. Despite pledges made by the Social Democrats, who de facto control the new government formally headed by Liberal Prime
Minister Nicolae Ciuca, the fiscal policy remains unclear. On the upside, the Social Democrats toned down calls to renegotiate the Recovery and Resilience Facility with the European Union.

The good news related to market indices provider FTSE Russel including two more Romanian companies in its indices didn’t help the market as a whole, despite the visible positive impact on the particular shares, One United (ONE) real estate group and waterways transport company Transport Trade Services (TTS). The shares of Romanian developer and investor One United surged by over 20% in less than a week, after FTSE Russell decided to include them in its FTSE Global All Cap index.

Other good news was generated by the listing of new companies on the BVB, such as transport and distribution company Aquila, which started trading on the BVB at the end of November after completing the biggest IPO of an entrepreneurial company on the Romanian stock exchange (€74mn).

The shares of the company started trading on the BVB on November 29 very close to the price of RON5.50 per share set in the IPO. Towards the end of the trading day, the price eased to RON5.46, consistent with a market capitalisation of nearly RON1.1bn (€220mn).

“Through the success of the primary public offering of Aquila, a market leader in the segment of distribution of consumer goods, we hope to raise awareness of other local entrepreneurs on the alternative of financing and developing their own businesses with the support of the local capital market,” said Olimpiu Blajut, deputy CEO of Swiss Capital, the brokerage house that intermediated the IPO and listed Aquila’s shares.

Romanian antivirus company Bitdefender prepares $2bn IPO in the US

Romanian IT security solutions producer Bitdefender, best known for its antivirus software, has hired investment banks JP Morgan and Morgan Stanley to help it with the launch of an IPO on the US market, Profit.ro reported.

The IPO would envisage a valuation of nearly $2bn for the Romanian company, according to sources familiar with the deal quoted by Ziarul Financiar daily. A successful listing would thus result in a second Romanian unicorn, after UiPath.

The procedures were reportedly launched in November.

The Romanian company has also decided that Bitdefender Free, one of the most popular free security solutions for Windows, will be permanently discontinued starting December 31. The mobile version operating systems Android and iOS are not subject to this decision.

In December 2017, the Vitruvian Partners investment fund bought a share of around 30% of Bitdefender. The company was then valued at over $600mn.

In the spring of 2019, Bitdefender appointed John Stynes, an Irish executive with nearly two decades of experience in listed technology companies, as CFO. At that time, the Romanian company was pondering listing its shares on the Bucharest Stock Exchange (BVB).

Bitdefender is a global computer security and antivirus software company, operating globally, which provides solutions to protect against cyber threats for over 500mn users in over 170 countries.

Founded in 2001 by Florin and Mariuca Talpes, the company is headquartered in Bucharest and has offices in the US, Canada, Australia, the United Kingdom, France, Germany, Spain, Denmark, Italy, Sweden, the Netherlands and the United Arab Emirates.

“The IPO would envisage a valuation of nearly $2bn for the Romanian company”
A mysterious video was uploaded to Telegram on January 7 showing four supposed terrorists with a Kalashnikov and a Kazakh flag who claimed to be members of a group called the "Kazakh Liberation Front", or KLF.

Speaking for the group, one of the four members went on to make political demands on the Kazakh state, using technology to distort his voice. All four were wearing ski masks and their eyes were obscured by black bars added to the video.

The spokesman said the group is actively fighting in various cities across Kazakhstan as part of the ongoing anti-government protests that broke out on January 2.

The group said the involvement of the Russia-led "peacekeeping" forces in the country’s civil unrest was the start of an occupation, encouraging citizens to “fight back, create resistance groups and organise attacks” against the Kazakh government and Russian military.

It didn’t take long for the video to break the confines of Telegram and go viral on Twitter. Conflict researcher @war_noir was one of the first English language accounts to share the recording, which had clocked 90,000 views at the time of writing. A number of Twitter users openly supported the group’s formation without questioning the authenticity of the footage.

The video is timely, as the KLF’s announcement came shortly after Kazakh President Tokayev blamed “foreign-trained terrorists” for the violent protests, and gave law enforcement the order to “shoot to kill without warning”. Residents in Almaty have been warned to stay at home after a curfew was imposed last week as “anti-terrorist” actions are being conducted.

Tokayev has also used the claims of an attack orchestrated by international terrorists to trigger Article 4 of the Collective Security Treaty Organisation (CSTO) that allows him to call on the other members to send military aid to restore public order.

And there is some evidence for terrorists acting in Kazakhstan. As bne IntelliNews reported, there has been plenty of footage shared on social media of civilians arming themselves, although a question mark remains over the authenticity of this footage.

The Kazakh authorities have been much more successful in their ability to control access to information in this crisis. Social media was allowed to operate unfettered during Ukraine’s EuroMaidan revolution in 2014, and Belarus’ President Alexander Lukashenko was unable to close down the Telegram messaging service during the mass protests in Minsk in the summer of 2020, which caused him a major headache. But the Kazakh authorities successfully shuttered the internet entirely during this protest. That gave it complete control of the information flow, as the population have only state TV and calls to relatives and friends to rely on to get information on what is going on.

The other source of reporting is Russian state-owned media and in particular, the only source of English-language reporting is the Kremlin’s flagship RT broadcaster. Both the Kazakh authorities and Russians have a vested interest in hamming up the conflict and the role of international terrorists in particular. As bne IntelliNews has reported, a Russian state-owned news agency TASS report of soldiers firing on protesters on Republic Square on January 5 appears to be fake, but has been widely reported on both state and international news outlets.

Getting accurate and verifiable information has been extremely hard. Two of the best known international correspondents who have been working in the country for years – Joana Lillis and Paul Bartlett – happened to be outside Kazakhstan on a Christmas break and have been refused entry on their return to report on the story. bne IntelliNews' own correspondent in Almaty is currently one of the only English-language reporters working on the protest story.

Amongst the many videos is one from January 5 allegedly showing protesters raiding an armoury, and photos released by the Kazakh Ministry of Internal Affairs the same day depicted numerous weapon seized from protesters, including
handguns and rifles. The existence of an anti-government militia sounds plausible.

Yet Tokayev’s claims of orchestrating “foreign-trained terrorists” didn’t have any basis until the appearance of the KLF video.

Many questions remain that undermine the authenticity of the video. The biggest problem is this is the first appearance of the group that has played no recorded role in Kazakh politics until now. If KLF are who they say they are, it is also the first documented militia group involved in the unrest. And the Kazakh authorities have released no evidence to back up their claim that international terrorist organisations are involved in the unrest, nor has it named the KLF as one of those groups.

Another red flag is the group’s use of Russian to deliver their message and KLF’s manifesto, published on its Telegram channel, is written in Russian. Although widely spoken, the country’s predominant language is Kazakh. A Kazakh patriotic group would presumably speak in their national language when encouraging violence against a foreign force, or at least have a Kazakh slogan, particularly when they are against what they call “Russian occupation”.

Several Twitter users also highlighted video claiming to show Ukrainian militants threatening terrorist attacks against the Netherlands. The investigative platform Bellingcat proved that the video was fake and likely staged by the Internet Research Agency, an institute infamous for churning out online disinformation and Kremlin propaganda. The video’s setting, timing and rhetoric, which includes the Ukrainian militants claiming to have “guys in the Netherlands ready to obey any order”, undoubtedly parallels KLF’s tone.

Others on social media said the spokesman’s accent is distinctly Ukrainian. A poll of native Russian speaks on Twitter conducted by bne IntelliNews sharing the video found that 40% of the respondents identified a Ukrainian accent, 24% said the accent was Russian, another 25% said there was no discernible accent, but only 10% said the accent was Kazakh.

The group is threatening to take action against the members of the CSTO force. A message sent on the evening of January 7 to the KLF Telegram channel threatens Belarusian CSTO forces. They allegedly know “all movements of the occupation troops on the territory of Kazakhstan, as well as personal data on the officers”, asking Belarusian commander, Colonel Dmitry Sobol, not to “carry out criminal orders” for his personal safety. They end the message with: “You are on the radar of our informers, and so far we are only watching. You have very little time left.”

In van Linge’s opinion, “a mysterious video where Kazakh insurgents are threatening violence against CSTO forces would be just what Putin and others needed to justify the very same CSTO forces being present in Kazakhstan” he said on his Telegram channel. “Since there are no known anti-government terrorist groups in Kazakhstan, the Kremlin needs to fabricate one into existence using a tried and tested propaganda campaign.”

Pro-Kremlin Twitter users latched on to the video and accused the US of backing the KLF, feeding into the popular disinformation narrative that the West is funding or agitating the protests. One of the Kremlin’s underlying narratives in any revolution or conflict is that Russia is there as a peacekeeper whilst a bellicose West surreptitiously intervenes to expand its sphere of influence.

Even if KLF are successfully proved to be fictitious, the Russian and Kazakh governments, and their supporters, will only denounce the investigation as Western propaganda, as was the case with the Flight MH17 and Skripal investigations. In this sense, the damage is done, and KLF’s video is already enough evidence to back their “foreign-trained terrorist” narrative.

The video continues to be shared online, although no mainstream media organisation has reported on the militia or its video so far. A few specialist or small media outlets have reported on the story: within the EU, a Cypriot news outlet with around 20,000 Facebook followers, Gegonotomikroskpio.com, published an article describing KLF as terrorists encouraging “civil war”. The website also promotes disinformation and conspiracy theories often propagated by the Kremlin, including COVID-19 and vaccine scepticism, as well as support for Belarusian autocrat Alexander Lukashenko.

The story has made a much bigger impact in Russian-language media. Multiple news websites report on KLF with absolute certainty of their existence, although these are still small outlets. The Russian news site The Daily Storm included a quote from Kirill Seymenov, a member of the Moscow think-tank Russian International Affairs Council, who seems to support the legitimacy of KLF: “I think there will be many more organisations. If people have a lot of weapons in their hands, they will of course try to turn into some kind of group.”

Another Russian website, Independent Gazette, stated that the rebels are Ukrainian military and that the voice-over has a Ukrainian accent, which in the Russian media world is a slur, as the Kremlin’s line is that the Maidan revolution in 2014 was orchestrated by far-right Ukrainian nationalists.

The various reports muddy the waters, a tactic the Kremlin has used to defang reports it is not happy with. So many versions of the story come out that at the end of the day the public don’t know what to believe any more. If it’s revealed that KLF does exist, then legitimate media have a hard job catching up with the baseless conspiracy theories already circulating online.

No credible source has verified the KLF existence so far. Its existence should be taken with a pinch of salt. Nevertheless, Russian and Kazakhstan state media are making hay from the release of the video. ●
Larry Cermak, the VP of Research at the Block, tweeted about the drop in hashrate. The Kazakhstan event is unlikely to lead to a decline in crypto prices, he said, adding that “it matters to estimate the impact of an unprecedented event like this.”

Hardware manufacturer Canaan has been looking to expand its crypto mining operations in Kazakhstan. It recently announced that it has deployed over 10,000 AvalonMiner units in the country.

Looking at the impact of the Kazakhstan events on BTC mining, *Fortune* magazine wrote: "The curtain just lifted on one of the many mysteries surrounding Bitcoin: How much is being produced using super-dirty coal in Kazakhstan. We knew that the Eurasian nation was a major destination for miners, and that the refugees recently expelled from China were flocking there." Still, it was difficult to establish how much of all the world's coins Kazakhstan was minting. Clouding the picture was the government's recent moves to severely restrict the mining boom that was plaguing its cities via rolling blackouts.

He added that btc.com estimated that Antpool, Poolin, F2Pool and Binance Pool witnessed massive reductions in their hashrate during the time the internet was shut down in Kazakhstan. He stated that “these are the pools widely used by Kazakh miners.

Russia’s e-commerce trade growth expected to slow to 10% in 2021

The volume of Russia’s e-commerce trade is expected to slow to 10% in 2021 after it expanded by the pandemic lockdown bump of 59% in 2020, Russian Online Retail Association (AKIT) President Artyom Sokolov told Russian newswire PRIME.

“In 2021, the e-commerce advance in the country was smooth, stable from month to month. The January–September results of RUB2.41 trillion [$322bn] are slightly above the same period of 2020 of RUB2.34 trillion,” Sokolov said as cited by PRIME.

Russia’s e-commerce was already booming before the epidemic struck, but an enforced lockdown that started in April 2020 that prevented people leaving the house and ordered them to minimise social contacts led to a major fillip for the burgeoning online retail business.
“A year ago there were several months of lockdown in the period when e-commerce was the only channel of almost the whole non-grocery retail for a long time, and, as a consequence, we saw abnormally high demand for goods on the internet. The figure of RUB2.41 trillion proves clients’ interest to the online channel – the patterns of the buyer behaviour that emerged during the tough restrictions in brick-and-mortar retail imposed due to the COVID-19 pandemic stay in force after their relief,” Sokolov added.

Russia’s online business has been growing at five times the rate of the real economy, but that growth is starting to slow now and the gap is also being closed at the real economic growth picks up as part of the post-COVID bounce-back.

The Russian economy grew 4.3% year on year during the third quarter, but the post-coronavirus recovery is almost over, say economists. “The solid 3Q21 figures were likely due to the still strong but waning momentum in retail and wholesale trade, manufacturing, and freight and passenger turnover,” Sova Capital said in a note.

At the same time, retail sales in the real world surged 5.6% y/y in September of 2021, accelerating from a 5.3% increase in the previous month, above market expectations of a 3.8% rise.

Nevertheless, online retail has still become a major driver of consumption and analysts say the pandemic has caused a permanent change in the way Russian retail works. Local online sales accounted for 86%, or RUB2.07 trillion ($26.8bn), but its share of overall retail trade has fallen by about one percentage point in the last year.

Logistic and supply change problems during the pandemic also knocked cross-border online trade, AKIT reports.

“In January-May, we saw stably falling volumes of cross-border trade, by 30% on average. There was a noticeable rise by 50-70% in July-September, but the cross-border market still failed to regain the position it lost with the breaking of the logistics chains due to the lockdowns,” Sokolov told PRIME.

In 2019, orders placed with foreign online stores accounted for 31% of the total e-commerce volume, but that plummeted to 14% in 2020 and was flat in January-September at RUB341bn ($4.6bn).

“In January-September, the share of online in total retail stood at 8.5%, but it will change by the end of 2021. It may beat the 2020 record of 9.6%. It can be explained not only by the new restrictive measures, which certainly boost e-commerce, but November and December are the traditionally high season in retail with sales and preparation for the New Year holidays,” he told PRIME.

**IPOs and strong results**

The boom in online retail in Russia has been fuelling a spate of IPOs as the major players list on domestic and international exchanges to raise further investment capital. Top five e-commerce site Ozon IPO in December 2020 was initially launched with the hope of raising $500mn but demand was so big the flotation raised a total of $1.2bn. In general Russia has been enjoying an IPO boom for move than a year, although recent burgeoning geopolitical tensions may have closed the window for further IPOs for the meantime.

Meanwhile the leading players continue to report strong sale volume growth, although not all the leading companies are actually in profit.

The Russian subsidiary of the Chinese e-commerce site AliExpress gross merchandise volume (GMV) increased by 36% on the year to RUB133.3bn in April–September,

“Russia’s online business has been growing at five times the rate of the real economy, but that growth is starting to slow now”
same period of last year, RBC business portal reported citing the data of InfoLine Analytics. As of the end of 3Q21 the share of top three players had expanded further to 36.5%.

The e-commerce market of goods sales is expected to reach RUB4 trillion ($55.1bn) in 2021 and more than double to RUB10.5 trillion by 2025, according to InfoLine.

As followed by bne IntelliNews, it was already suggested that the "big four" Russian e-commerce operators AliExpress Russia, Wildberries, Ozon and Beru are set to outgrow the market and face imminent market consolidation, while internet major Yandex is also emerging as highly competitive e-commerce contender.

In 2020 the three largest e-commerce marketplaces were Wildberries (RUB437bn), AliExpress Russia (RUB229bn) and Ozon Holdings (RUB197bn). In the meantime, InfoLine estimates that Ozon has already beaten AliExpress in 4Q20 in terms of turnover.

In comparison to Europe and Asia, Russia’s Internet retail is about five years behind the other countries, Sokolov said.

“Taking it and online volumes in other states into account – 32% of total retail in the UK, 27% in China, and 14% in the US, the Russian e-commerce market has one of the highest growth potentials,” the AKIT chief said.

Romanian software producer Arobs lists shares on Bucharest Exchange

The shares of Romanian software developer Arobs Transilvania Software have been listed on the Bucharest Stock Exchange (BVB) and closed the first trading day, December 6, at a price of RON1.94 – 43% higher compared to the private placement.

Arobs Transilvania Software was founded in 1998 by its current CEO and main shareholder Voicu Oprean.

At the closing price of December 6, the company has a capitalisation of RON884mn (€176mn) and is traded at a PER ratio (compared to the profit of RON40.4mn in 2020) of 22x.

The company sold a package of 54.7mn shares in a private placement held in October 2021, accounting ex-post deal for 12% of the company’s capital, for a total price of RON74.2mn.

The private placement and listing of Arobs shares were carried out with the support of BRK Financial Group.

Arobs specialises in providing customised software solutions, based on the latest technologies, and also has multiple software solutions that have a strong presence on the Romanian market and in Central and Southeast Europe.

The company is headquartered in Cluj-Napoca, with regional operational offices in Bucharest, Iasi, Targu Mures, Baia Mare, Suceava and Arad, as well as seven branches abroad.

In 2020, Arobs Transilvania Software registered, at an individual level, a turnover of RON154.5mn, an Ebitda of RON46.6mn and a net profit of RON40.4mn.

For the year 2021, the company estimates revenues at a consolidated level in the Arobs Group amounting to RON192.7mn and consolidated Ebitda of RON52.8mn.

“The company currently has over 950 employees and collaborators and provides services and software solutions to over 8,000 customers in 14 countries around the world.

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Avito becomes world’s most visited classified site

NEO

Russia’s Avito topped Similarweb’s list of most visited classified advertisement sites for November 2021, in a sign that emerging markets are taking the lead in this fast-growing sector.

Classified ads, which date back to newspapers in the eighteenth century, have moved online and are rapidly becoming one of the largest digital marketplace channels. The ease of listing, low price and ability to target your specific audience make classified ads websites a disruptive technology, especially for small businesses hoping to make a splash.

While America’s Craigslist is the most recognisable online classifieds platform, it’s in emerging markets that the segment is really taking off. According to digital analytics service Similarweb, the most visited classified ads website in the world for November 2021 was Russia’s Avito, which displaced Craigslist from the top spot for the first time.

Avito is billed as Russia’s leading classified ads website, where users can do everything from buy and sell second-hand items to find a job, rent a home or buy a car. The site had almost 280mn visits throughout the month, according to Similarweb. The average visitor stays for 11 minutes, in which time they visit around 12 pages of advertisements.

“Avito is a unique phenomenon in Russia: it has become a household name, like Google worldwide,” said Avito’s CEO Vladimir Pravdivy, commenting on the rating. “This has all become possible because Avito is the country’s largest and most secure platform for meeting a wide range of everyday needs, from buying and selling goods and cars to finding a job and services, renting a home, and much more,” he added.

With six deals made every second, Avito is the most downloaded shopping app in Russia, according to analytics company App Annie. The platform is so popular that a new profession – avitolog – has sprung up in Russia: someone who makes their money on Avito. Some observers attribute this popularity to the rise of conscious consumption in Russia, with people increasingly opting to buy used items or re-home the items they no longer need.

Where most classifieds sites are vertical (exclusively posting adverts related to a certain industry, like jobs or used cars), Avito is a horizontal site which subdivides its listings into a collection of vertical categories. This allows it to benefit from the consumer traction of horizontal platforms while maintaining the pricing power and economies of scale characteristic of a vertical site. Meanwhile, Avito’s integrated delivery service can ship items across Russia’s vast territory from Kaliningrad to Vladivostok, allowing dealers to benefit from the relative lack of infrastructure in Russia’s more remote regions.

Classified advertisements site Sahibinden is the third fastest-growing technology company in Turkey, according to Deloitte. Like Avito, it embraces a range of verticals, from cars to apartments. It also benefits from the growing appetite for environmentally friendly consumption in Turkey. The company is part of the Leaders for Climate Action community, aiming to make the technology industry carbon neutral.

In fact, by fighting fast fashion and encouraging the sale and re-use of second-hand goods, the classified advertisements segment is naturally in step with a growing focus on sustainability. Russia’s Avito calculates that it saved 267 gigajoules of energy and 123 cubic metres of water in 2020 alone by encouraging the second-hand market and preventing the need for new products to be made. It also saved material equivalent to 23 landfill sites from going to waste in the same year – a particularly important theme in Russia, where waste solutions are sorely needed.

In addition to giving a new life to used goods, Avito and other classified advertisements sites also offer new goods, and you can even buy a small business on the site, like a café or a barbershop.

Another emerging-market player, Brazil’s Olx.com, saw trading profit up 139% year-on-year in Q4 2021 as internet traffic soared. It recorded particularly strong performance in motors (with 69,000 car transactions in Q4) and real estate, which signifies a shift in consumer preferences towards buying properties and cars via digital formats. This may be partly down to the expansion of pay-and-ship services, which increase consumer confidence and trust in the arrival of their product on time and in a good condition.

This dynamic segment remains very young, and it is set to keep growing in emerging markets as penetration increases. A survey of market players conducted by Mitula Group found that 84% of participants felt positive about the next few years for the market. The possibilities for future developments are endless, with big data opening up the potential for tailored advertisements or new services designed to grow brand awareness for new companies.

Classified advertisements might call to mind the back pages of a pre-war newspaper, but they’ve returned with a vengeance in a digital guise. Pandemic or no pandemic, this format isn’t going anywhere.
Russia's $6.5 trillion decarbonising plan will launch next year

Ben Aris in Berlin

Russia is revving up to launch a four-decade-long, RUB480 trillion ($6.5 trillion) investment campaign to reduce carbon emissions by 60% before 2050 from 2019 levels, of which RUB89 trillion ($1.2 trillion) will come from public funds.

President Vladimir Putin offered an optimistic scenario of Russia’s attempts to reduce its CO2 emissions during his speech at the Russia Calling! Conference on 30 November. The president said Russia could reach carbon neutrality even earlier than the 2060 target if all the goals in the plan are met on time. The country has “a whole set of tools for reducing the economy’s carbon intensity” and a comprehensive roadmap will be ready by March 1, 2022.

The president also promised Russia will develop renewables and hydrogen projects (including green hydrogen), and will benefit from the current large share of low-carbon generation in the mix.

“The country should also use the absorption potential of its forests, fighting forest fires more effectively and growing new forests,” said Putin, highlighting a big part of Russia’s plan to reduce its emissions.

Russia is about to launch a 40-year-long campaign to make the country carbon neutral by 2060 that will cost about $1.2 trillion.

Then on July 1 next year Russia will formally launch a massive climate initiative with the goal of reaching carbon neutrality by 2060. A new programme of energy efficiency will also be finalised by October 1, 2022.

After a slow start a string of environmental disasters in 2021 seems to have woken the Kremlin up to the dangers and encouraged it to grasp the nettle. As bne IntelliNews has reported, Russia’s permafrost is melting and could cause over a trillion dollars worth of damage to the Russian economy.

Russia has a relatively good starting point as, featured in the Cost of carbon in Russia, the collapse of the Soviet Union and the subsequent investment into modern equipment and technology have already seen emission levels fall dramatically over the last three decades. And on top of that, Russia is home to the largest forests in the world. But at the same time, it also hosts some of the most polluted places on the planet and any emissions by Russia are big emissions, as the country is so vast. Russia has a key role to play in the fight to avoid a global warming catastrophe.

The rate of temperature rise in Russia is now triple that of the global average. This summer was plagued by wildfires over territories the size of European countries.

In addition, warming weather led to a power unit belonging to Norilsk Nickel spilling over 20,000 tonnes of oil into Arctic rivers in the Pyasino region in June 2020, which was declared a federal emergency by the Kremlin and cost Norilsk $2bn in fines. Also in June 2020, a once-in-a-1,000 year snow melt flooded the TGK1 power station near Murmansk, putting two of its hydropower units out of action. A few months later, in October 2020, an unusual algae bloom off the coast of Kamchatka killed all sea life along several kilometres of coastline. And most recently Russian oil major Lukoil spilled 100 tonnes of oil in the Komi Peninsula, although very little of that got into the local rivers that flow into the Barents Sea.

Costly reductions
Decarbonising Russia is going to be expensive. The effort, so far, has been led by Russia’s leading corporations after some found their shares excluded from Scandinavian pension funds.
for their poor environmental, social and governance (ESG) scores. For example, the world’s biggest nickel producer, Norilsk Nickel, spent over $2bn on cleaning up its act but complained that the money spent “adds nothing at all to the bottom line. It’s pure cost.”

VTB issued a report that looked at some of the cheaper and easier things Russia can do to reduce its emissions and estimated they can be reduced by a quarter for a price tag of RUB43 trillion (the equivalent of 1.3% of GDP per annum), and 50% of them for RUB86.6 trillion (2.7% of GDP per annum).

“In comparison, cutting 100% of emissions would require an astronomical RUB479.8 trillion by 2060 (or 15% of GDP),” VTB Capital (VTBC) analysts Vladimir Sklyar and Anastasia Tikhonova said in a report “ESG & Decarbonisation.”

“The cheapest ways to achieve these targets include tackling waste disposal, reducing emissions, decarbonising the power sector and undertaking forestry projects. These account for 59% of total emissions in Russia and can be decarbonised for RUB102.7 trillion ($1.4 trillion), we estimate. That broadly matches MinEconomy’s RUB88.8 trillion 60% CO2 reduction programme. Transport remains the most expensive sector to decarbonise, followed by cement and iron ore & steel,” the analysts said.

As these investments are pure cost they will come with price rises to close the gap. The most substantial price hike to foot the CO2 removal bill is required in the power (28% end-user price increase) and cement (40%) sectors, says VTBC. Decarbonising the oil & gas and metals & mining sectors would have a minimal effect on product pricing, the bank adds.

“Full decarbonisation requires annual capex at 5x annual EBITDA for transport, 2-3x for cement/chemicals, 1-1.5x for the power sector and waste, and less than 1x for oil & gas and M&M, keeping the dividend prospects in these sectors the highest in the economy, which is going through a green transformation,” VTBC said.

One of the key issues is what price the cost of carbon is set at, as this is the mechanism that has been adopted to price the cost of reduction and how to pass these costs on to consumers and government. A market for carbon has emerged in Europe and it currently values the cost of carbon at $50 per tonne, but governments are still setting prices arbitrarily, with the Scandinavians putting the cost at over $100 per tonne but poor countries like Ukraine estimating the figure at under $1.

At the start of the year Russia launched an experiment on the island of Sakhalin where it introduced market mechanisms for costing carbon that put the price at around $25 per tonne. Putin said in a speech this week that the Kremlin was ready to expand the experiment to other regions in Russia. But Russia has yet to launch the all important carbon trading system, where the price of carbon is the keystone.

“Our research indicates that Russia can halve its emissions using a carbon price of only $30/tonne. After the quick wins by 2030, the CO2 removal capex is set to rise as decarbonisation activities move away from methane and the power segments,” VTBC said.

During his speech at Russia Calling! Putin also said that he has ordered the Ministry of Finance and Central Bank of Russia (CBR) to work out tax credits, subsidies and guarantees for companies undertaking green projects also by March 1, 2022, when a register of climate projects will be finalised.

The cost of the programme means that MinFin and the CBR will play key roles, as the spending is bound to be inflationary at a time when Russia is already struggling to contain rising prices. “We think that 40-year decarbonisation could add as much as 12% to the real price increase (or a proportionate margin contraction),” the analysts at VTBC estimate.

**Looking for cheap solutions**

With its abundance of cheap fuels of all kinds and the wasteful habits of the Soviet era Russia is the third-biggest emitter of GHGs in history on a cumulative basis.

Russia’s officials are now looking for the cheapest ways they can find to decarbonise and adopting a “technology neutral” approach, where anything goes as long as it works.

Another factor going into the mix is some projects will actually make money, such as recycling projects or burning waste for fuel rather than dumping it in a methane-generating landfill, and these programmes can go ahead without the need for carbon pricing or a trading system.

“Russia is capable of delivering significant quick wins, even without decarbonisation capex rising significantly from present levels.”

“Russia is capable of delivering significant quick wins, even without decarbonisation capex rising significantly from present levels. Existing power sector investments planned until 2030 could lower the energy CO2 intensity 21% and waste management can be decarbonised with a negative cost, while oil & gas and coal companies can fit the CO2 reduction costs into their existing capex programmes (as regards methane emission reductions). Forestry projects also remain a competitive way of national decarbonisation,” VTBC said.
The Ministry of Economy’s plan so far is spread across a number of sectors, but is concentrated on improving energy efficiency and management, eliminating emissions through leakage, and undertaking various forestry projects. The most expensive heavy capex version of reducing emissions is going to be put off until later, after 2030.

“The cheapest decarbonisation options in Russia are still cutting methane emissions (in both oil & gas and coal mining), reducing the power sector’s footprint (through a greater share of renewables) and forestry projects. These three areas account for 59% of gross national emissions, on our estimates, with the full decarbonisation of these industries costing RUB102.7 trillion in capex,” VTBC said.

The oil, gas and power companies will bear the brunt of the costs in the first stage, but reducing their methane leakage will be negligible for the hydrocarbon producers.

The greatest effect on consumers from these investments is going to be the upward pressure on electricity prices. VTBC estimate that end-user electricity prices would need to rise 28% to accommodate sufficient decarbonisation funding for the sector (in a 100% scenario).

Later on, the mining and transport sectors are going to be the expensive ones. VTBC estimated that transport alone will consume a third of the entire RUB480 trillion that is going to be invested, or about RUB145 trillion, as the railways will have to replace its entire ICE fleet with electric vehicles.

However, costs will go up everywhere. With a focus on avoiding the capex-heavy solutions, the answer will be to improve energy efficiency and savings everywhere. That means things like new regulations for washing machines to force them to switch to more efficient motors, better waste management, retooling factories everywhere and investment into construction efficiency. And decarbonising households is one of the most expensive options for the economy and unlikely to start at the beginning, as those costs will fall on the public. “We do not anticipate any rapid decarbonisation of the average Russian household until 2060,” says the VTBC analysts.

A large share of these costs can be pushed on to the companies and VTBC estimates they will add some RUB74 trillion ($54bn) in annual additional payments for the goods and services. All this together will probably send prices up by about 12%.

“Our study shows that full decarbonisation would require a significant step-up in investment across the sectors (except for oil & gas). For some sectors, such as power, transport and chemicals, this step-up might translate into a two-three-fold increase in investments. However, we note that the existing CO2 reduction targets are milder and can generally be dealt with as part of Russian corporates’ announced investment programmes (except for the power sector),” says VTBC.

All this spending will also be a heavy burden on Russia’s investment case, as it will eat into free cash flows that are currently being paid out to dividends to shareholders; Russia currently has the highest dividend payout yields in the world – about twice those of the MSCI EM benchmark average.

As much of the capital expenditure will actually borne by companies and not the government, the amount of money they will have invest will also eat into their profits. VTBC estimates that in most sectors the current capex spending in most companies’ business plans is insufficient to cover the necessary investments to reduce emissions by the required amount. The extremes are in oil & gas, where the companies have plenty of money and the investments are relatively cheap, and the power sector, where the investments are huge and could wipe out the sector’s entire profits.

**Government’s targets**

The government, of course, will also play an important role and has targeted boosting Russia’s renewable energy capacity and expanding its already extensive nuclear power production. Despite the legacy of Chernobyl, Russia’s nuclear technology is now considered to be world class and Russian nuclear exports are booming as a result.

The government also plans to significantly step up forestry projects and launch wide-scale carbon capturing, predominantly by oil & gas companies. Further down the line more of Russia’s hydrocarbon reserves will be re-tasked from a fuel for export to become the feedstock for a hydrogen production business. Although decarbonisation measures are planned in other sectors as well, the lion’s share of the activities will be concentrated on measures to keep Russia’s CO2 abatement curve relatively low.

“MinEconomy’s intensive decarbonisation strategy envisages using the best and most efficient technologies, with measures to introduce, replicate and expand low and carbon-free technologies, encourage the use of secondary energy resources, change the tax, customs and budgetary policies, and develop green finance,” the VTBC analysts said.

“There are also measures to preserve and increase the absorptive capacity of forests and other ecosystems, and support technologies for capturing and utilising greenhouse gases [GHGs]. The strategy requires GHG emissions to be reported, rather than the requirement of the potential carbon pricing and trading quotas (the preliminary version envisaged it coming into operation after 2030, at RUB500-700/tCO2e),” VTBC concluded.

MinEconomy estimates that by 2050, this would make it possible to cut emissions 60% from the 2019 level and 80% from the 1990 level. The total investment for decarbonisation is estimated at 1% of GDP in 2022-30 and 1.5-2.0% in 2031-50. The additional growth in GDP due to this investment is expected to exceed the spent funds by 25%.
Richard Lockhart in Edinburgh

The nuclear lobby, meanwhile, is strong, with energy ministers from Bulgaria, Croatia, Czechia, Finland, France, Hungary, Poland, Romania, Slovakia and Slovenia speaking out in October to support nuclear’s inclusion in the taxonomy.

The issue is dividing EU members, with France and a number of nuclear CEE states, such as the Czech Republic, Hungary, Bulgaria and Romania, in favour of including atomic energy and natural gas, while Germany is leading a group that also includes Italy, Spain, Denmark, Austria and Luxembourg that is against including gas and nuclear in the green taxonomy.

Pro-gas and pro-nuclear countries regard gas as a transition fuel that can help reduce emissions in countries such as Poland and the Czech Republic that are now aiming to reduce coal’s role in power generation.

The nuclear lobby, meanwhile, is strong, with energy ministers from Bulgaria, Croatia, Czechia, Finland, France, Hungary, Poland, Romania, Slovakia and Slovenia speaking out in October to support nuclear’s inclusion in the taxonomy.

The taxonomy is part of the EU’s Green Deal and aims to create a concise and clear list of economic activities that can be considered sustainable and green. This is a key instrument in Brussels’ attempts to prevent greenwashing and to focus green investments on effective projects.

The EU wants the new taxonomy to create investment certainty for companies, investors and policymakers.

Weak European sustainable financing rules would particularly affect those economies lagging behind in the transition towards climate neutrality. The EU taxonomy is therefore one of the most important policy tools to get right and enable a post-fossil energy transition in the central and eastern parts of the bloc.

However, the role of nuclear and gas in any green taxonomy will be a major political issue, particularly given the momentum provided by the COP26 conference towards reducing fossil fuels’ role in the energy sector, and especially a move away from coal.

The EU’s green taxonomy is a crucial benchmark and reference point for defining what projects and investment are green or not, and will form the foundation for a green bond standard that will be used to issue €250bn as part of the EU’s post-pandemic recovery fund.

The International Energy Agency (IEA) has said that there can be no new investment in gas-fired generation, and that existing gas-fired power plants will have to be phased out by 2035 in the OECD and 2040 globally.

The role of gas is further complicated by the current volatile nature of the European gas market, with high prices and a recent political row with Russia over supplies and the signing of new long-term contracts.

Put simply, Russia would like to sign more long-term contracts with its customers with CEE and in Germany and Austria, while the EU wants to reduce the role of such contracts as part of a move to a more market-based gas supply model.

The EU also published legislation, which formed the second part of its Fit for 55 energy package, that would increase the role of hydrogen in European gas markets and reduce methane emissions.

“Weak European sustainable financing rules would particularly affect those economies lagging behind in the transition towards climate neutrality”
Bonum continues investment spree with Russian coking coal

NEO

Investment fund Bonum Capital has bought a 16% stake in metallurgical company Koks, Russia’s largest producer of merchant coke and among the world’s cleanest coking coal plants.

The shares were acquired from a minority shareholder, marking the resolution of an ongoing dispute between the shareholder and the fund, according to Kommersant. Bonum Capital has not disclosed the amount it paid for the shares.

Coking coal is used in industry as a raw material for the production of pig iron. Metallurgical giants in Russia are currently looking for ways to make their operations greener, with the steel industry currently responsible for between 7-9% of global CO2 emissions, according to the World Steel Association.

“We believe that PJSC Koks is a leader and one of the most promising players in the metals industry in Russia, and we see great prospects for effective growth, taking the company to a whole new level,” said Murat Aliev, founder and owner of Bonum Capital. “In the medium term, we believe the company has potential to expand into international capital markets,” he added.

Green technologies are being harnessed worldwide in the drive to clean up this polluting industry. Swedish steelmaker SSAB made history this year with the first pilot delivery of carbon-free steel, for example. It was produced using renewable energy and hydrogen in an electric arc furnace (EAF). Russian businessman Alisher Usmanov announced this week that green technologies will transform European metallurgy, one of the rationales for his own investment in hot briquetted iron, a raw material for the production of steel which can generate up to 35% less CO2 than traditional manufacturing methods.

The deal continues a series of investments by Bonum into promising sectors of the Russian economy. Earlier this year, the fund invested $150mn into Russian forestry major Segezha Group after taking part in the company’s IPO. The move marked a vote of confidence in the Russian forest product sector, with Segezha itself set to become the country’s largest forestry assets holder after an expected M&A with another industry player.

Bonum Capital is an international investment firm which invests in a range of assets, from venture capital and private equity to Russian real estate. According to its website, the firm specialises in investing on public markets. The company also has expertise in acquiring distressed assets, cleaning them up, and packaging them alongside the assets of other industry players in order to grow their value.

This article first appeared in New Economy Observer (NEO), a digital publication covering the intersection between finance and social responsibility, with a special focus on emerging markets. It offers news and analysis on major issues shaping the new global economy, including climate change and renewable energy, sustainable development, e-commerce and tech innovation, and the future of work.
UKRAINE — NO WAR TODAY, AND PROBABLY NONE IN FUTURE
The Ukraine Crisis is approaching its first birthday – the 1st Guards Tank Army first “came to rest” 250 km north of Ukraine’s border in April 2021, sparking what has been a long and strident chorus of invasion alarms. Back in April I wrote an analysis of Russia’s options and likely course of action, which measured the probability of an invasion at “nil”. So far, it has been nice to be right, if rather lonely.

The mainstream media have consistently cried that invasion is imminent, and have firmly anchored that trope in the mass mind that Russia’s troop formations are lined up on Ukraine’s border just awaiting the “go” signal. In contrast, the facts are that Russia’s troops are stationed some 450 km by rail from the border, are in “camp” formation, with equipment parked in regular lines like cars outside a supermarket, and with personnel rotating to and from their normal bases.

Moscow has repeatedly and firmly asserted that it will not invade Ukraine. Russian public opinion (reported extensively in bne IntelliNews and elsewhere) is firmly against an invasion of Ukraine. Ukrainian public opinion is also largely of the view that an invasion will not happen. Even President Zelenskiy himself has gone on record saying “there is no reason for panic”, and describing an invasion as “not imminent at all”.

Ukraine’s Security Council Secretary Danilov echoed his President, saying he could see no evidence of an impending Russian invasion, and he told the BBC’s Ukraine service that he believes that the crisis is a product of domestic political pressure in the West.

Finally, Ukraine’s Defence Secretary said he had no intelligence at all implying an invasion. He went on to reject explicitly a UK report that Russian forces had formed up into 60 “strike groups” for an attack on Ukraine – a report that appears to have flowed from Boris Johnson’s inability to distinguish between a Strike Group and a normal Battalion Tactical Group – the cool modern name for a good old infantry battalion.

These messages are beginning to penetrate to the desks of the leaders of Germany, France and Italy. Chancellor Scholz has prevented Germany from supplying weapons or ammunition to Ukraine, has effectively vetoed a plan to isolate Russia from the SWIFT secure bank transfer messaging system, and has sent emollient noises east.

President Macron, meanwhile, is publicly pushing Kyiv to start delivering on the legal obligations it took on under the Minsk agreement, pressing the use of the Normandy Four format as a forum in which to move these forward. Execution of the Minsk Agreement will inevitably lead to legalised autonomy for the Luhansk and Donetsk Oblasts of Ukraine, which is why Kyiv has so far refused to act on it.

And as if those dove-ish actions were not enough, Prime Minister Draghi last month told a press conference that there was little Europe could do to help Ukraine, either militarily or economically, and that it should just maintain “a state of engagement” with Moscow.

In contrast to these relaxed and non-confrontational stances, the Anglophone club has increased both the volume and quantity of its alarm calls; from the recall of embassy staff and families from Kyiv, through the supply of large quantities of Javelin missiles and launchers to Ukraine by the United Kingdom, to the forward deployment of a handful of front-line aircraft and warships, and (yesterday) to a notification from the Pentagon shortening the deployment notice of two brigades of US troops from ten days to five.

These symbolic Anglophone moves have been accompanied by a stream of hysterical rhetoric, spiced with an invented Russian “plot” to set up an unknown Ukrainian politician as a puppet President after a successful invasion – a plot described by Sir Tony Brenton, former UK Ambassador to Moscow, as “…ill sourced, internally contradictory and frankly implausible”.

In sum, we have a picture in which one arm of Nato’s members – the Continental Europeans – are heading one way, while the other – the Anglophones – are heading in the opposite direction. Setting apart the feeling of satisfaction which must be prevalent in President Putin’s office at this (intended) result, the interesting question here is “Why”? Why are the Anglophone members of Nato working so hard to persuade the populations of Europe and the United States that Russia plans to invade Ukraine?

We are forced to speculate, but some evidential data points can be seen. In Washington, President Biden’s administration is suffering a critical loss of credibility and popular support, in part due to the humiliation of the Afghan withdrawal (and in small part due to his evident cognitive decline).

Mr Biden badly needs (a) to look tough, and (b) to get a firm win for team USA against either Russia or China. One way of looking tough against Russia is to lead the American people to believe that Russia is indeed planning to invade Ukraine, and then to stop that plan in its tracks by the exercise of US power.

If the White House has come to the same conclusion that I have – that Mr Putin has no intention of invading – then it becomes quite rational to pump up the threat to hysterical levels, to allow
events to take their course (no invasion), and then to claim the credit for a successful deterrence operation.

US policy is also, always, influenced by profit. US companies have built a long string of liquefaction trains to export liquefied tight methane to consumers around the world. At present the EIA estimates that total US export capacity is in the region of 140-150bn cubic metres per year. The original intention was to supply Asian buyers – Europe was always seen as a small potential market since it can buy cheap pipeline gas in large quantities from Russia, Algeria, Norway, the UK and Denmark.

But setting Europe at odds with Russia upsets one leg of that competitive threat, and potentially opens the door to large-scale supplies of LNG from the United States, at highly profitable end-prices and with much shorter (and more profitable) voyages from the Gulf of Mexico. The volumes of production available are highly material in the context of Europe’s gas import demand, though with the snag that a single large LNG carrier can deliver only about 0.1 bcm per voyage, creating bottlenecks both in ship-availability and in gasification terminals. The margins on offer are eye-watering. US tight gas leaves its liquefaction train at about $8 per mmBtu, while in Europe gas is currently wholesaling for around $30 per mmBtu and touched $38 at the end of 2021. If US producers supplied just 50 bcm of European gas, and if wholesale prices moderate by a third, to $20 per mmBtu, the net profit on offer would be around $1bn per month.

In London the agenda is probably more personal where the Prime Minister is struggling for his political life.

In this context it is also important to remember that Nato and Europe are not coincident. Seven EU states (Finland, Sweden, Ireland, Malta, Austria, Cyprus and Croatia) are not members of Nato, but do have foreign policy weight which might be used to pull other European states away from Nato and towards Brussels. Anglophone aggression will add to that pull.

There is an old Civil Service saying – “never let a good crisis go to waste”. It seems that all of the key players in this crisis are making good use of it.”

The White House and Downing Street are not the only beneficiaries of hysteria. Sitting quietly in the background all this time has been the European Commission. Here the underlying agenda flows from Articles 25 and 26 of the Lisbon Treaty. Article 25 mandates that the EU shall have a common foreign and security policy, and Article 26 mandates that member states shall (not may) give it effect under the direction of the High Representative (the EU’s Secretary of State).

So far, EU member states have completely ignored both articles, but the Commission plays a long game. In order for the Articles to gain real living force it is necessary for the influence of Nato (polluted in the Commission’s view by the relative military weight of the three Anglophone states) to diminish. For that to happen, Nato must be seen to have failed in some material and critical way.

The leadership’s case to MPs is partly that it would be highly dangerous to be leaderless at a time when the United Kingdom might find itself at war. It is therefore firmly in the interests of Downing Street to inflate the risks of a major conflict to the maximum, while knowing (as does Washington) that it can later stake a claim to successful deterrence, whose credit will accrue to… Mr Johnson.

In London the agenda is probably more personal. Here the Prime Minister is struggling for his political life under charges of hypocrisy and outright lying over whether Downing Street followed its own stringent coronavirus (COVID-19) infection rules in 2020. Few outside Parliament believe Mr Johnson’s narrative.

Inside Parliament only 100 of the 358 Conservative members of the House of Commons have signed a letter of support for Mr Johnson (and it must be remembered that approximately 100 members of the Commons are also members of the Government at any one time). Mr Johnson’s chances of surviving as leader and Prime Minister rest on two circumstances – his ability to win a future election, and the fact that Nato is in a crisis over the future of Ukraine. The leadership’s case to MPs is partly that it would be highly dangerous to be leaderless at a time when the United Kingdom might find itself at war.

The Commission must be quietly hoping that the Ukraine crisis will provide that failure, as the foreign policies of the Anglophones and Europeans visibly part company and the resulting geopolitical stress leaves Europeans shivering in their homes this winter for lack of gas.

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“In London the agenda is probably more personal where the Prime Minister is struggling for his political life”

“Here’s a plan, Boris.”
Can Russia cut off gas supplies to Europe?

Ben Aris in Berlin

With the US threatening Russia with “massive consequences” if it invades Ukraine, Russia has threatened to take “military and technical” action in response. Is cutting Europe off from gas deliveries one of the Kremlin’s options? Some analysts say that would be like detonating a nuclear bomb, with the same mutually assured destruction for both sides.

Russia’s use of gas as a political weapon has become a common trope following Gazprom’s decision to cut off Ukraine’s gas supplies in the winter of 2009 and there have been at least two less significant episodes since then.

However, the Kremlin has protested that in the “gas war” with Ukraine in 2009 it was simply shutting down supplies because Ukraine was stealing gas from the pipelines and unable to pay the bill.

“It was a force majeure situation,” Igor Shuvalov, the first deputy Prime Minister, told bne IntelliNews in an interview at the time. “They couldn’t pay their bill, so we cut the supplies. It’s a perfectly normal practice.”

Whatever the truth of the matter, the decision to plunge not only Ukraine into darkness, but many EU countries that depend on transit gas for power and heating, did tremendous reputational damage and almost certainly accelerated European efforts to diversify gas supplies, which has since morphed into a drive to switch to renewables.

But Europe is still heavily dependent on Russian gas, which makes up between 30% and 40% of the energy mix in any given year. Gas in European storage tanks just fell below 40% this week, its lowest level in the last five years. As bne IntelliNews reported, Europe is on course to end the heating season at the end of March with the tanks only 10% full – just enough to scrape through this year, but even if Russian supplies were cut off then Europe would be unable to refill them and would face a major energy crisis next year that would make this year’s gas crisis, caused by a V-shaped market, look like child’s play.

“Such a crisis… would almost certainly include rolling electricity blackouts as well as a massive shortage of heating (gas is directly used for heating in many European homes and business and can’t easily be replaced by other fuels). European consumers would literally be freezing in the dark before being hit with power bills very few could afford to pay,” warns Roland Smith, the senior oil and gas analyst with BCS GM. “The truth is, Europe has no substitute for Russian gas.”

And thanks to the Ukrainian gas clash Europe has already made a great deal of progress in diversifying away from its dependence on Russian gas. When deliveries started in the 1970s Russian gas made up some 70% to 80% of supplies; however, the share has fallen steadily since then and Russian gas currently accounts for just under 35% to the total, but even that is vital to keeping the lights on.

“The “gas weapon,” to the extent it exists, can be viewed like nuclear weapons: “Too powerful to ever be used” or, for that matter, to even be mentioned directly in negotiations over this or that disagreement between countries,” argues Smith. “Rather, such weapons are best left in the background, with everyone fully understanding that they exist and that by existing, they limit the scope of escalation of disagreements in international relations.”

While shutting off the gas spigot would have enormous and immediate effect in Europe, the long-term consequences for Russia’s gas business make it an extremely unappealing option for Moscow. The problem is that gas deals usually run for decades and so the reputational risks are key to the business. And Russia has over a hundred years worth of gas reserves under the ground in the Yamal complex in the Arctic.

Part of what has been driving this year’s gas crisis has been Russian President Vladimir Putin’s insistence that Russia won’t ramp up gas deliveries beyond its contractual obligations unless Europe signs off on new long-term contracts. Russia has been investing heavily into developing both the fields and also
the infrastructure – the controversial Nord Stream 2 gas pipeline specifically connects the Yamal fields directly to Germany, Gazprom’s biggest customer – but needs long-term contracts to make this business profitable and viable. Taking the long-term view, the Kremlin is uninterested in making a few extra bucks from the spot market in Holland during the recent soaring price for gas if it can lock in solid profits for the next 30 years.

Despite its history with Ukraine, Gazprom and Putin have repeatedly insisted that Russia is a “reliable energy supplier.” Indeed, during this winter Gazprom has scrupulously stuck to the terms of all its supply contracts. And when it transited less than the 65bcm of gas it signed off on in a new transit deal with Ukraine in December 2019 the Russian state-owned company simply paid the transit fees for 2020.

“Keep in mind that since the start of Soviet-German gas contracts in the early 1970s, the mind-set of the Russian side has been “meet the contract at all costs.” At one point, experiencing some technical problems, the Soviets reportedly even cut Leningrad off from gas for a few days in order to make sure the export contract was fully filled,” says Smith. “Times change, of course, and a couple of hiccups have been experienced over the years, but I think this prioritisation is pretty deeply embedded in Gazprom’s corporate culture (although, obviously, decisions of such magnitude would be taken in the Kremlin, not Gazprom headquarters).”

Smith speculates that if Gazprom were to do the 2009 clash with Ukraine over again it would now choose to keep the gas flowing, as the decision to cut Ukraine off has already done significant damage to its business and continues to cause major problems in getting those crucial long-term contracts signed now, 13 years later.

“I think Russia is extremely unlikely to purposefully cut Europe off from gas,” says Smith. “I think the Kremlin is fully aware that such an action would have long-term consequences for Russia, the cost of which are impossible to calculate but would almost certainly exceed the value of any short-term gains.”

**What if war broke out?**

While the Kremlin has repeatedly denied it has any intention of attacking Ukraine, what would happen if Russia did invade is neighbour?

There is a high chance that the Druzhba (Brotherhood) gas pipeline would be damaged or destroyed in a Russian onslaught. Even if only a smaller flare-up occurred, contained in the already disputed Donbas region, there is a tangle of gas pipelines nearby that could get caught up in the conflict.

Given the Kremlin would try and sell this war as a “local conflict” as both the US and Nato have said clearly they will not send troops in to protect Ukraine, then the Kremlin is likely to keep the gas flowing to Europe and make the clear distinction between Planet Business and Planet Politics, as *bne IntelliNews* has reported on many times.

That means ramping up supplies via the Yamal-Europe pipeline across Belarus and Poland from near zero now to 100% to help offset the loss of Ukrainian transit. Smith speculates that Gazprom may even simply turn on Nord Stream 2 without regulatory approval, which has been ready to start operations at short notice for months already, as an emergency measure and just pay the fines later. Europe may even accept this decision simply to keep the lights on.

Could LNG fill the gap? While LNG deliveries provide yet another way to diversify away from Russian piped gas, the LNG business is still too young to make much of a difference. Gazprom sells between 180 bcm and 200 bcm a year to Europe, which is equivalent to a third of the total LNG production. However, many countries in Asia, such as Japan, are entirely dependent on LNG for their gas. Diverting enough of this gas away to supply Europe – about half the total supply – would send LNG prices skyrocketing and cause a major energy crisis in Asia, says Smith.
Ukraine together with Russia is one of the world’s biggest grain exporters and already the main source of wheat for many developing countries. A Russian invasion of Ukraine would smash its agricultural sector, with the shock waves rippling out across the world.

Agricultural reforms and the development of the business has been one of the few bright spots in the economy in recent years and the export of grain has become the largest source of foreign exchange earnings for the budget.

The country has been enjoying bumper harvests in recent years and Ukraine set a new record harvest in 2021 for the fourth year in a row.

Ukraine exported $27.9bn worth of agricultural products in 2021, almost a quarter more than the previous record $22.4bn set the year before in 2020, according to the Institute of Agrarian Economics.

At the same time, in 2021, the share of agricultural products as a percentage of total Ukrainian exports decreased from 45% in 2020 to 41%, partly thanks to soaring commodity prices, especially metal, while grain exports maintained their record-breaking growth rate.

Agriculture Minister Roman Leshchenko said in December the country harvested a record 84mn tonnes of grain in clean weight in 2021, up from 65mn tonnes in 2020.

Of the total grain output, Ukraine exported roughly 18mn tonnes of wheat out of a total harvest of 24mn tonnes in 2020, making it the world’s fifth-largest exporter.

And this year will be even better. Ukraine has exported 33.2mn tonnes of grain so far in the 2021/22 July-June season, up 25.7% from the same stage a season earlier, Ukraine’s Agriculture Ministry data showed as of the start of January, reports Reuters.

The ministry said the 2021/22 exports are on track to include 24.5mn tonnes of wheat this year, allowing exports at the end of the agricultural marketing year in June to be even bigger than in the last two years.

"The country has been enjoying bumper harvests in recent years and Ukraine set a new record harvest in 2021 for the fourth year in a row."
After Ukraine turned away from Russia since the annexation of Crimea in 2014, trade with Europe has soared. Ukraine already ranks fourth in the supply of agricultural products to the EU and 14th in terms of agricultural imports from EU countries.

But the unintended benefit of breaking off trade relations with Russia has been the rapid diversification of Ukraine’s exports worldwide. In particular, it has developed new trade deals with North Africa and the Middle East.

Amongst the main customers are China, the EU and Lebanon, but the largest consumer of Ukraine’s wheat is Egypt, which imported more than 3mn tonnes in 2020 – about 14% of its total supply.

Ukraine wheat imports also account for between a fifth and a quarter of the wheat imports of Malaysian, Indonesian, Bangladeshi and the Middle East, according to FAO data as cited by Foreign Policy.

This year the harvest should be even better and could break the record yields for the fifth year in a row, according to agricultural experts. The cold winter has covered the fields with snow, which is good for crops, protecting them from the frost.

With 42mn hectares of farmland covering 70% of the country and about 25% of the world’s reserves of black soil, Ukraine’s agribusiness sector remains the most promising sector of the economy.

But Ukraine’s very success in building up global wheat exports could turn out to be a major headache for the rest of the world if the current showdown with Russia comes to blows.

Blood on the black earth
Ukraine was famous as a Soviet breadbasket. Its “black earth” regions have some of the most fertile earth in the world, but most of these regions lie in the east of the country – Kharkiv, Dnipropetrovsk, Zaporizhia – that would all be the first to be overrun by an invading Russian army should war break out. The most exposed is the Kherson oblast, which lies just west of Donetsk and Luhansk, where an undeclared war with Russia has already been raging for seven years.

Russia’s troops are massed in bases close to Ukraine’s eastern border, so the grain producing regions are the first ones that an invading force would reach.

While bne IntelliNews has reported that a full-scale invasion is highly unlikely, smaller-scale military operations remain more than possible. One scenario that would affect agricultural production that is possible is for the Kremlin to flood the Donbas with more weapons and scale up the conflict in Donbas, which would not require Russians soldiers to cross the border but could see fighting extend beyond the current line of contact and so affect farming in the neighbouring regions – something that the Kremlin has suggested in the last week it is contemplating.

An escalation could seriously disrupt Ukraine’s agricultural production and that would only exacerbate the global inflation in food prices, which is already a major economic headache for central bankers everywhere.

It would cause price hikes in the cost of bread and other staples in a number of countries like Libya, Yemen and Lebanon that are all already heavily dependent on Ukraine wheat imports but not stable economies.

The nightmare scenario is that this could recreate the conditions that sparked the Arab Spring at the start of the last decade that were caused by a sharp jump in food prices. Currently food price inflation is already on a par with that of the Arab Spring era in Tunisia and Egypt.

“Last time global food price inflation was running as hot as in 2021 was 2011, setting the scene for the Arab spring,” tweeted Adam Tooze, an academic with Columbia University.
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**RUSSIA**

**Political outlook**

A host of factors including the adverse economic effects of the coronavirus (COVID-19) pandemic, an ageing population and capital flight have converged to create a nightmare scenario for Russian economic policymakers. While the economy bounced back in 2021, all the challenges that Russia has been facing over the last decade remain in place for 2022.

The rapid economic growth which Russia enjoyed in the 2000s following the transition to a market economy has slowed considerably over the past decade. 2021 has been no exception, with lockdowns and other restrictions related to the coronavirus pandemic further hindering any prospects of Russia’s economy finding its feet. Policymakers have been left in an unenviable position, attending to competing demands in an economy beset by challenges.

Russia’s petro-dollar economic growth model was exhausted in 2013 when growth fell to zero despite oil prices still being over $100 at the time. The Kremlin has failed to grasp the nettle and make the deep structural reforms needed to invigorate its economy and has in the meantime fallen into the middle income trap.

The Kremlin is not blind to the problem and in 2018 launched the 12 national projects that are supposed to “transform” the economy, but a series of external shocks in the form of the collapse of oil prices in 2020 and the pandemic have conspired to delay work and investment.

A consensus among economists suggests that investment in innovation and infrastructure in high-productivity sectors will be an essential component of successful economic policy in Russia. Existing development plans like the National Priority Projects (first announced in 2005) and the Unified Development Plan to 2030 (recently approved, but yet to be published) were designed with this aim in mind, hoping to nurture the sectors which have the greatest growth potential and the most overspill into other areas of the economy.

With the economy bouncing back following the corona crisis Russia is in its best position in years to make progress on the reform front in 2022, but it remains to be seen if the political will is there. While the necessary reforms are obvious and the plan is in place, where Russia always falls down is on the implementation.

**Macro economy**

The Russian economy recovered to pre-pandemic levels in 2021 after its sharpest contraction in eleven years of 3% in 2020. But it may now face headwinds from a possible drop in prices for oil, its main export, and numerous interest rate hikes.

The latest Russian Economic Report from the World Bank expects Russian growth to slow in 2022 and 2023 after a rebound of 4.3% GDP growth in 2021. The Bank revised its 2022 GDP growth forecast downwards from 2.8% to 2.4%, while seeing the growth slowing down to 1.8% in 2023.

The EBRD also cut Russia’s outlook for 2022 to 3% in November, citing risks from a possible drop in oil prices in 2022 and the impact of the coronavirus variants.

The World Bank named the four main risks to the Russian economy: the pandemic, an unexpected surge of inflation, international sanctions, and, in the long term, green energy transition. Low rates of vaccination in Russia make the pandemic a particularly large threat to the economy.

As followed by *bne IntelliNews*, the Russian economy grew 4.3% year on year during the third quarter of 2021, but the post-coronavirus recovery was almost over by the autumn.
In a report on regional economic prospects, EBRD said the Russian economy is boosted by social spending programmes that are facilitated by higher commodity revenues. Geopolitical tensions, notably the risk of further sanctions, connected to military tensions on the Ukraine border, also weigh on growth prospects.

EBRD’s forecasts are in line with those of the Russian central bank that expects gross domestic product (GDP) to grow by 4.0-4.5% in 2021 and by 2.0-3.0% a year in 2022-2024.

“Geopolitical tensions, notably the risk of further sanctions, connected to military tensions on the Ukraine border, also weigh on growth prospects”

Inflation remains the biggest challenge for the Russian economy in 2022 but one that it already had well in hand as 2021 came to a close.

The Bank of Russia is way ahead of the curve with monetary tightening. It was one of the first central banks to start rate hikes and one of the first to realise that inflation is not just a temporary phenomenon. By now, the rate hike cycle in Russia is almost done and remaining hikes are apparently fully priced in by the financial markets.

Russia is likely to face a dilemma between supporting higher growth and fiscal stability. If choosing the latter, Russia could attempt to promote infrastructure spending and encourage the private sector to participate. The recovery in oil production could be the primary driver in 2022, contributing nearly 1ppt.

To encourage households to save, CBR could hike the key rate to 9% by 1Q22 before easing it to 8% by YE22. Higher commodity prices and the attractiveness of the carry trade in Russia vs. other EMs should make the rouble a bright spot in 2022. Geopolitical turbulence and the global strength of the US dollar are likely to interfere with the rouble’s potential appreciation, which analysts expect to fluctuate around a RUB/$ rate of 71-72 in 2022.

Markets outlook
Russian banks and companies are awash with money, having had their most profitable year in a decade in 2021, partly driven by the post-COVID bounce-back. But many analysts are also arguing that the world is at the start of a new business super-cycle and that Russia is especially well placed to benefit from it.

“Essentially, financial trends in the corporate sector suggest that we are at the beginning of a classic economic cycle. The onset of an economic cycle is a much better explanation of the current economic developments than simplistic references to COVID-related disruptions, which are almost certainly going to disappear,” VTB Capital [VTBC] argued in an end of year note.

“Yes, COVID played its role as a trigger of the economic cycle, but the economic impact is going to last much longer than the pandemic itself. Soaring margins are set to launch an investment cycle and we are already seeing this in corporate capex plans. No one can say for sure how long this cycle might last, but it is quite unlikely to roll over before the new capacity goes online,” VTBC said.

On top of that, the rise in oil and commodity prices has put the Russian government back into profit earlier than expected and the country is running a triple surplus once again – trade, currency account and federal budget.

For the equity market all these factors will conspire to make Russian stocks appealing again. After lying moribund since the sanctions regime was imposed in 214 and the RTS index trapped in a trading band between 900 and 1,300, the stock market broke out in 2018 and rallied strongly in 2019. Again the pandemic postponed the rally, but it quickly resumed in the last quarter of 2020 when the vaccines appeared and the RTS touched a decade-long high of 1,900 in October 2021, but ended 2021 at 1,593 after a sell-off on the back of rising geopolitical tensions.

Despite a sell-off in the last months of 2021 due to renewed geopolitical tensions, most analysts expect the stock market rally to continue in 2022 and have an end-of-year RTS target of 2,000.

“Many analysts are also arguing that the world is at the start of a new business super-cycle and that Russia is especially well placed to benefit from it”
UKRAINE

Ukraine’s economy bounced back strongly in 2021 following a deep recession in 2020 caused by the coronavirus (COVID-19) pandemic, but by the summer that growth was slowing more than expected as the low base effects wore off.

Ukraine’s economy is still working well below potential due to the low investment, lack of progress with reforms and the ongoing conflict with Russia that are hurting the business climate and dissuading investors.

Ukraine has attracted very little foreign direct investment (FDI) as although incomes are now rising much more quickly, the country’s risks remain very high, as illustrated by the talk of war with Russia Rolf, owned by Sergei Petrov and the free rein given to the country’s oligarchs.

“Ukraine’s economy is still working well below potential due to the low investment, lack of progress with reforms and the ongoing conflict with Russia that are hurting the business climate and dissuading investors”

FDI fell from a recent peak of $5.2bn in 2019, the last year of strong growth, to a mere $215mn in 2020 and remains depressed due to the political instability. The government’s poor treatment of investors into the renewables sector – one of the only sectors to have attracted substantial foreign investment – has also weighed on the investment climate and has stymied the investment into green power that was ongoing.

The one area where Ukraine has successfully attracted some foreign investment is in retail, where several large multinational retailers such as Sweden’s IKEA and Germany’s METRO have moved in. These companies are early movers in transition economies and their arrival is an encouraging sign, as it says they believe that Ukraine is at the beginning of long-term sustainable recovery. However, the pace of that recovery continues to disappoint.

Renewable energy investors were attracted by the generous green power tariffs offered by the Poroshenko administration. However, the tariffs proved to be too generous and the government has failed to meet its obligations, running up a $1bn debt for unpaid power bills. That was settled finally in the fourth quarter of 2021 with the issue of a Eurobond by the state-owned power company Ukrenergo, but the failure to pay and the government’s attempts to retroactively renegotiate the tariff hurt Ukraine’s already poor investment image.

The problems have led to various downgrades for Ukraine’s growth outlook. The government downgraded its official forecast for 2021 from 3.4% from the 4.1% predicted in April. Economic growth in 2022 was also downgraded slightly to 3.6% instead of 3.7%. According to the Ministry of Economics, the revision of indicators is mainly due to the slowdown in investment growth and challenges and threats of post-pandemic development.

IMF downgraded Ukraine’s GDP growth estimate to 3.2% from 3.5% in the October forecast. However, the IMF has left Ukraine’s economic growth expectations in 2022 unchanged at 3.6%, and in 2023 at 3.4%. And JP Morgan sharply downgraded its forecast from 4.5% to 2.3% in 2021, while maintaining an expectation of 5% growth in 2022.

Inflation has been the main macroeconomic problem. After crushing inflation in 2019, which fell to a post-Soviet all-time low of below 2% in May 2020, inflation soared back in 2021 to peak at 11% in September before starting to fall as a series of aggressive rate hikes began to take effect. The outlook for inflation is to end at 10.6% in 2021 before falling to 6.5%, according to the official forecast.

“The one area where Ukraine has successfully attracted some foreign investment is in retail, where several large multinational retailers such as Sweden’s IKEA and Germany’s METRO have moved in”
POLAND

After a turbulent 2020 and 2021, marked by the pandemic – it has cost Poland 100,000 lives already – a presidential election, and a multitude of internal and external conflicts, underpinned by growing macro-economic problems, 2022 appears unlikely to offer any relief.

Poland is about to enter another election cycle amidst the apparently accelerating disintegration of the Law and Justice (PiS) led government, fighting an increasing number of battles at home and abroad. That promises utter politicisation of pretty much everything, a trend that will be exacerbated as PiS is shattering ever more norms and the once untouchable principles on which Poland has been built over the past three decades.

Politics will be underpinned by the macro-economic environment to a large extent, because of accelerating inflation and a rising cost of living – traditionally the bane of Polish governments.

Poland’s relations with the EU will continue to be tested in the context of Brussels’ trying to make PiS roll back its flagship judicial reforms. Another conflict will continue over the EU’s climate policy, which the government has blamed for the drastic increases in Poles’ electricity bills.

The turmoil in the east – the perceived threat of Russia invading Ukraine, the possible revival of the migration crisis on the border with Belarus, and Moscow manipulating gas prices in winter months – will add to the overall sense of instability, possibly fuelling a complete remodelling of Polish politics beyond the currently taken for granted confrontation between the PiS and the liberals from the Civic Coalition (KO).

While Poland is not holding any elections in 2022, the country will be gripped by the prospect of one the following year. With the ruling camp’s engine sputtering more and more often, as the government hinges on a fickle majority of two in the parliament, the next year in Polish politics will be a permanent campaign ahead of the 2023 vote.

The increasingly dysfunctional government will face ever more problems next year: the likely persistent inflation, the fallout of the coronavirus (COVID-19) pandemic, the spiking costs of energy are challenges that even the most effective administration would have a hard time handling.

It appears, however, that the ruling coalition of Law and Justice (PiS), United Poland (SP) plus some more or less obscure groupings and individual MPs is losing its ability to make sustained – even if divisive – decisions.

That, at least in theory, should fuel the opposition’s efforts to consolidate ahead of the election and offer voters an alternative after years of merely reacting to what the PiS-led government has been doing.

The Hungary-style consolidation of the opposition around a single candidate for a post-PiS prime minister is out of the question, however, as fault lines run too deep. The best strategy appears, then, for the opposition to run in two large blocks, one liberal-leaning, the other more centre-left.

The government’s position is made more complicated by internal differences, especially when it comes to its relationship with the European Union. While PiS is indeed making its routine EU-sceptic noises, it also is looking out to Brussels to prop up economic growth with the pandemic relief fund and the bloc’s next budget. PiS also softened its stance on the EU during the migration crisis on Poland’s border with Belarus, choosing the “we are defending Europe” tone in its handling of the crisis.

But PiS’ coalition partner, United Poland, is taking its Euroscepticism utterly seriously, refusing to move an inch over the issue that is defining Poland’s open conflict with Brussels: the rule of law. That puts PiS in a bind, as without United Poland the ruling coalition would collapse overnight.

It remains an open question if the government will crack under more pressure in 2022 or, conversely, consolidate around the overarching goal of winning a third term in office. The opposition, in turn, is expected to go beyond its anti-PiS strategy to draft a positive offer, possibly looking to win over the growing numbers of voters ditching PiS to join the “I don’t know” camp in the election polls.

The polls still show the coalition leading at an average of 37%, according to data canvassed by Politico Europe’s poll of polls. The centrist-liberal Civic Coalition is at 24%, followed by another centrist group, Polska 2050 at 15% – with both tipped to work closely together in the run-up to the election and quite likely after it.

The far-right Konfederacja averages 9%, while Lewica – which could join the liberals in the possible future government if PiS loses – lingers at 7%. The agrarian Polish People’s Party is at 4%, just under the 5% threshold needed to win mandates in Parliament. Support for other parties is smaller than the statistical margin of error in the polls.

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CENTRAL EUROPE AND THE BALTIC STATES

Central Europe faces a critical year in 2022, with a key election in Hungary in April in which Prime Minister Viktor Orban, the region’s high-profile strongman, is seeking a fourth consecutive term, while rumbling political instability in Poland and Slovakia could lead to early elections. This could be a make-or-break year for the region’s radical right-wing political forces, which will have an impact right across the EU and the Balkans.

These potential political changes come as the region, especially the Baltic states, faces a much more dangerous geopolitical environment, as neighbouring Russia menaces Ukraine and tightens its grip on Belarus.

Central European states – which already have some of the highest deaths per capita from coronavirus (COVID-19) in the EU – are also bracing for the sweeping eastwards of the Omicron version, at a time when businesses are already struggling to recover, government budgets are under huge strain, and people are increasingly ignoring restrictions or even marching against them.

Political instability and social unrest could also be worsened by rises in inflation, energy prices and interest rates. These will hurt living standards – which have stagnated since the global financial crisis – and slow down Central Europe’s already protracted convergence with Western European levels.

International politics

The radical right-wing governments in Budapest and Warsaw remain locked in conflict with Brussels over a range of issues sparked by their attempts to consolidate their rule – notably by limiting judicial independence – and pursue populist culture wars against sexual minorities that violate EU values. Orban’s Hungary is also in the dock for rampant corruption and its failure to prosecute it.

The European Commission finally seems to have found a credible weapon to fight the populist contagion by threatening to hold up financial flows if the rule of law is breached and EU money put at risk. Unless the Commission cravenly back down, it is difficult to see a solution to this impasse until there is political change in both countries, something that still unfortunately appears uncertain.

Warsaw and Budapest have also become more isolated in the EU following the electoral defeat of populist governments in Slovakia in 2020 and in Czechia at the October 2021 general election, as well as the replacement of German Chancellor Angela Merkel by a centre-left coalition. The Visegrad Group of the four Central European countries, which Orban has weaponised in his battles against the EU, looks likely to become increasingly moribund now, though the V4 might still occasionally unite to fight Brussels’ policy on climate change or on migration, if there is another wave.

Hungary faces becoming more and more isolated and irrelevant in the EU, not least over foreign policy, where it continues to pursue closer relations with Beijing and Moscow at a time when, following the German election, the bloc is more and more united on the threat both countries pose.

Domestic politics

Radical right-wing parties have been a malignant cancer in Central Europe since Orban returned to power in 2010 determined to build a semi-authoritarian regime to entrench his rule. He was joined by Jaroslaw Kaczynski’s Law and Justice Party (PiS), which closely followed his lead after it won the 2015 Polish election. Both governments have formed a united front to oppose the EU’s values, and have tried to encourage similar political forces in neighbouring countries, the Balkans and across the EU.

Radical right-wing populism continues to be fuelled by social disparities created by the transformation from communism, the cultural shock from accession to the EU and its values, as well as phantom fears about migration and other topics spread by misinformation. But this year both radical right-wing governments face their toughest challenges yet as Orban confronts a united opposition and the ruling Polish coalition continues to crumble.

Both governments have struggled to cope with the COVID-19 pandemic, partly because they have been reluctant to impose tough restrictions, which would have been unpopular with their often elderly and rural voters, many of whom have refused to be vaccinated because of distrust of the state as well as online misinformation.

In Poland the vaccination rate is around 57%, the worst in Central Europe after Slovakia, whose take-up is just 48%. Hungary’s vaccination record is better – at 63%, roughly the same as the Czech Republic – but the country has the second-worst death rate in the EU after Bulgaria. In the Baltic states, vaccination rates are higher still – with Lithuania and Latvia achieving almost 69% – but their current infection rates are among the worst in the region.
With their voters frustrated by the continuing COVID-19 restrictions and the soaring cost of living, both radical right-wing governments have tried to divert attention by reviving fears over migration. This has had diminishing success – the influx of several thousand refugees from Belarus to Poland last year seems to have done little to boost PiS support. Now both governments are turning more to cultural issues such as abortion and homosexuality to whip up support, which is bringing them once again into conflict with EU values.

Opposing them, civic organisations have led huge protests and opposition parties have forged wide coalitions, usually led by centre-right parties (with the region’s left-wing parties out of power and marginalised).

The Slovak opposition mobilised to oust left-wing populist Robert Fico in 2020, and the Czech opposition joined in two coalitions of the centre-right and the centre to defeat ‘technocratic populist’ Andre Babis at the 2021 election. Poland’s opposition parties may form centre-right and left-wing coalitions ahead of the general election there in 2023. Meanwhile in Hungary, after three election defeats the opposition has finally united and will fight April’s election under one list and one candidate for premier, the liberal conservative Peter Marki-Zay.

Orban is currently ahead in the opinion polls ahead of the April 3 general election, which will be fought on a very crooked playing field, with a gerrymandered electoral system, as well as a great imbalance of campaign funding and media coverage. If Orban wins a fourth consecutive term, this will likely embolden him to become even more obstructive towards the EU; if he is defeated, this would mark a dramatic political shift in the region back to liberal democratic values.

Poland could also have an exciting political year if Kaczyński’s PiS calls – or is forced to call – early elections as its coalition crumbles. At the moment it too is ahead in the opinion polls, but in both countries the political mood could change as the cost of living crisis worsens and the pandemic drags into a third year.

Nevertheless, populism – whether of the right, centre or left – remains a powerful force in the region, and it could even mount a return in some countries that have already shaken it off.

The Slovak coalition is also looking fragile as the split between the two right-wing populist parties and their centre-right partners widens, though it is expected to try to stagger on as long as it can, given the lead in the opinion polls for the two rival left-wing opposition parties of onetime allies Robert Fico and Peter Pellegrini. Unless the government can somehow pin corruption on top figures in the preceding Smer government in which both premiers served, its chances of staying the distance and retaining power at the next election look slim.

In Czechia all eyes will be on the candidates for the January 2023 presidential election, with a real risk that Andrej Babis, the agro-chemical billionaire and former premier, will triumph. He may be given a helping hand if the new centre-right government goes too fast in cutting the budget deficit. This could also enable Babis’ “technocratic populist” ANO party to return to power at the first attempt at the next general election.

In Latvia, the October general election is anticipated to increase political fragmentation, with a raft of new populist parties jostling to enter the Saeima. Populism is also on the rise in neighbouring Lithuania as well as Estonia, where the far-right EKRE party is riding high over migration fears.

Macroeconomic environment

Over the past two years Central European governments have been helping businesses and employees cope with the economic impact of the pandemic; now, as their economies begin to recover fast, they are starting to be concerned about the rise in budget deficits and public debt and are considering tightening their belts, even though the pandemic is still far from over.

On top of this challenge, businesses and households are coming under new pressure from rising inflation, energy prices and interest rates, which are crimping margins and hurting living standards. Budapest and Warsaw are now imposing price caps on energy and other staples, but these moves will only have a short-term effect. Inflation is expected to hit 10% in Poland in February.
SLOVENIA

Slovenia is heading towards general elections in spring 2022. This will pit the government led by Prime Minister Janez Jansa – who critics say is taking Slovenia down the same illiberal route as Hungary and Poland – against the opposition parties determined to unseat him.

The pressure on Jansa to resign stepped up in 2021, with the opposition parties accusing him of degrading Slovenia’s democracy, not respecting the rule of law and tightening his grip on the media. He has also clashed several times with EU officials. President Borut Pahor plans to call a general election for April 24 as the earliest possible date and to sign a decree on the election date in February.

Four opposition parties, the List of Marjan Sarec (LMS), Social Democrats (SD), Levica (the Left) and Alenka Bratusek’s Party (SAB), signed a cooperation agreement on September 28, agreeing to form a government without Jansa’s rightwing Slovenian Democratic Party (SDS) should they gain enough votes in the next general election.

Under the deal the opposition parties agreed to “normalise” Slovenia, to form a government without the ruling SDS and the parties supporting it, and that a prime minister-designate will be put forward by the participating party which has won the most votes. Levica described Jansa’s government as destructive and anti-democratic, and accused it of pursuing far-right policies.

Jansa came to power in March 2020 after the resignation of Marjan Sarec at the end of January 2020. The government consisted of the SDS, the Modern Centre Party (SMC), New Slovenia (NSi) and the Pensioners’ Party (DeSUS), but DeSUS left the coalition in December 2020 due to disagreements with Jansa.

Ahead of new elections in 2022, support for Slovenia’s minority government has been falling. The most recent public opinion poll conducted by Mediana Institute showed that only 16.3% of respondents would support the SDS, while 59.7% of them rate the work of the government negatively.

Under Jansa, Ljubljana has frequently been in conflict with EU institutions, which came under the spotlight during Slovenia’s six-month EU Council presidency in the second half of 2021. Recently, Slovenia has been criticised by EU officials for the delay in appointing two European delegated prosecutors (EDPs) and for cutting funding for news agency STA. The two EDPs were finally appointed by the European Public Prosecutor’s Office (EPPO) on November 24.

Jansa’s government cut off funding for STA at the end of 2020, after the prime minister accused it of unfair reporting. STA is supposed to receive funds for its public service activities. The European Commission has repeatedly expressed serious concerns about this issue.

The finances were restored in November 2021, when the new acting director of STA Igor Kadunc and the head of the Government Communication Office (UKOM) Uros Urbanija signed a deal on the provision of STA’s public service, valid until the end of 2021.

During 2021, protests against anti-COVID-19 measures imposed by the government were frequent in Slovenia.

The government has been tightening measures and is trying to get more people vaccinated to prevent the spread of the pandemic after it faced a severe fourth wave of COVID-19 epidemic in October and November 2021 that peaked at over 4,000 daily cases on November 17.

Following the spring general election, Slovenia will hold presidential and local elections in the autumn.

Presidential elections are due in October 2022. The incumbent Pahor is ineligible to run as he has served two five-year terms.

Local elections have a fixed date on the third Sunday of November. The local elections rarely reflect political realities at the national level as many candidates in the country’s 212 municipalities are elected from local lists without a firm party affiliation, or from smaller parties that are not represented in parliament. In the last election, the People’s Party (SLS) ended with the largest number of mayors despite being absent from national politics since 2014.

Macroeconomy

Growth is set to moderate in 2022 following strong GDP growth figures in 2021 from the low base in 2020.

The European Commission has downgraded Slovenia’s GDP growth forecast for 2022 by 0.9 pp to 4.2% and growth is expected to slow down further in 2023 to 3.5%, following projected growth of 6.4% in 2021.

For 2022 the IMF projection for Slovenia’s economic growth was lifted by 0.1 of a percentage point (pp) to 4.6%.

In the first nine months of 2021, Slovenia’s GDP expanded by an annual 7.4% and domestic demand is expected to remain the main growth driver.
The central bank said that the growth is expected to be slightly slower in the final quarter of 2021, particularly in light of the potential expansion of containment measures to prevent the renewed spread of the pandemic. Furthermore, the risks associated with the poor epidemiological picture in Europe, the spread of the new coronavirus variant, bottlenecks in supply chains, and high energy prices and input commodity prices are all growing.

External environment: The country’s current account surplus is projected at 6.4% of GDP in 2021 and 6.3% of GDP in 2022 following a surplus of 7.4% of GDP in 2020, according to the IMF.

Slovenia posted a current account surplus of €1.56bn in the first nine months of 2021, which is down by 37.6% from the same period in the previous year, according to central bank data. In 2020, Slovenia posted a current account surplus of €3.3bn, which is up by 20.2% from 2019.

In the third quarter of 2021, net exports had a negative contribution to the GDP growth of 5%, on account of the stronger increase in import compared to exports. With a high level of investment, including in inventories, import growth was significantly above export growth.

According to Erste Group, Slovenia’s current account surplus is seen at 4.5% of GDP in 2022 from 4.8% of GDP in 2021.

Foreign direct investment (FDI) is expected at 2.4% of GDP both in 2021 and 2022, according to Erste.

Inflation and monetary policy: Inflation has been rising, which the central bank attributed to several one-off factors. It reached 4.9% in December, of which higher prices of petroleum products contributed 1.3 pp. The recent rise in energy prices is attributable to a low-base effect, and high prices of oil and natural gas on international markets, while prices of emissions allowances are also rising.

The expectation is that inflation will persist at higher levels over the coming months, until the situation eases in global supply chains and on the energy markets.

Slovenia’s harmonised index of consumer prices inflation is seen at 1.7% in 2021 after the country posted an average deflation of 0.3% in 2020, the European Commission said. Inflation is expected to further speed up to 2.1% in 2022 and to slow down to 1.7% in 2023.

In terms of average annual inflation, the IMF said that Slovenia’s consumer prices are seen rising by 1.4% on average in 2021 and to speed up to 1.8% in 2022, compared with a slim deflation of 0.1% in 2020.

Industrial production: The situation in industry remained favourable, although firms are reporting high capacity utilisation and shortages of intermediate goods, which is already curtailing growth in exports, according to the central bank. Firms are also seeing growth curtailed by higher commodity prices and energy prices, and a shortage of skilled labour. Quarterly growth in value-added in industry thus slowed to 0.5% in the third quarter of 2021. Other sectors saw current growth in activity either maintain the same level as in the second quarter, or pick up the pace.

Year on year, industrial production increased by 6.2% in October, after rising by 7.8% y/y in September.

In October 2021, the total value of stocks in industrial production was 1% higher than in September 2021. It was 9.6% higher than in October 2020 and 10.6% higher than in October 2019.

Real economy
Retail: The growth of retail sales is expected to slow down to 7.3% in 2022, from estimated 14.8% growth in 2021, according to Erste.

Slovenia’s retail sales soared by an annual 34.3% in October, accelerating significantly from a 17.1% y/y growth in the previous month.

Retail sales also grew compared to pre-pandemic October 2019, by 20.1%. The annual growth was primarily a consequence of the increase in retail trade with automotive fuel (by 97.2%), but growth was also significant in retail trade of non-food products (by 13.1%) and food products (by 7.6%).

Banks: The net profit of Slovenian commercial banks plunged by an annual 38.3% to €324.4mn in the first nine months of 2021, the Bank of Slovenia said. This was a result of lower non-interest income.

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MOLDOVA

Politics
After pro-EU candidate Maia Sandu defeated the pro-Russian incumbent Igor Dodon to take Moldova’s presidency in December 2020, her Party of Action and Solidarity (PAS) won a clear majority in the parliamentary elections of July 13, 2021. A government was quickly appointed, headed by Prime Minister Natalia Gavrilita.

Upon gaining majority support in parliament, President Sandu and her party announced thorough reforms in the judiciary, starting with external evaluation of judges and prosecutors. General prosecutor Alexandr Stoianoglo has been suspended and investigations were launched against him. But the process was hasty and created the impression of poor coordination and superficial legal justification of the actions, allowing the opposition to criticise the process.

Speaking of the opposition, Andrei Nastase’s Dignity and Truth Party (PPDA) has expressed moderate support and frequent criticism in regard to the new PAS government. Currently not holding any MP seat, the PPDA can be regarded as “the pro-EU opposition” to the government. The “pro-Russian opposition” is formed by Dodon’s Socialist Party, which joined forces with Vladimir Voronin’s Communist Party.

The electorate’s overwhelming pro-EU vote in the last two elections was followed by political and financial support for Moldova from EU institutions and individual countries, particularly from Romania. The European Commission and Romania resumed the assistance programmes suspended in the past for deviations from the path of reforms and extended financial support to Moldova to mitigate the effects of the COVID-19 pandemic. In November, the Commission extended a €60mn grant to help the country overcome the natural gas crisis created by Gazprom cutting the gas supplies by one third.

Moldova’s relationship with Russia is in the process of normalisation, after Dodon attempted to bring Moldova closer to the political and economic organisations controlled by Moscow, primarily the Eurasian Economic Community (EEC). The new government in Chisinau discontinued the country’s participation as an observing member to EEC meetings while concomitantly intensifying diplomatic ties with the European organisations, pinpointed by Sandu’s frequent visits to Brussels and other European countries. Foreign Minister Nicu Popescu visiting Moscow expressed cautious and moderate positions, seen by some as too moderate particularly in regard to the Russian troops in the Moldovan separatist republic of Transnistria.

Macroeconomy
GDP growth: The Moldovan economy grew by 10.3% y/y in the first three quarters of 2021, fully reversing the slowdown in 2020. Compared to the first three quarters of 2019 (before the crisis), Moldova’s economy expanded by 1.2%. It is a small advance, yet more than initially expected.

Most sectors of the economy performed well: agriculture generated 14% y/y more value added, construction +5.3% y/y, industry +9.8% y/y and IT & C +11.9% y/y.

Domestic demand still relies to a large extent on imports. Consumption (+11.5% y/y in January-September) and gross fixed capital formation (+7.9% y/y) taken together exceeded the country’s GDP by 28% in the three quarters.

Imports, expressed in comparable prices, rose by 23% y/y — more than three times faster than exports (+6.5% y/y).

For the whole year 2021, growth may end up exceeding the official 6% forecast and even the 6.8% forecast of the World Bank or the 7% projection sketched by the European Bank for Reconstruction and Development (EBRD).

For 2022, the government expects 4.5% growth, slightly more than the EBRD’s 4% forecast. The low base effects and the resumption of external financing support expectations for even stronger performance depending, however, on further waves of COVID-19 that may defer investment projects by foreign manufacturing groups that will likely seek to develop or relocate to Moldova new production facilities.

External environment: Moldova’s current account deficit widened by 14% y/y in the third quarter of 2021, to $400mn. The deficit in the four-quarter period ending September 2021 increased to $1.57bn, from $1.52bn calculated three months earlier. Compared to the four-quarter period ending September 2020, the current account (CA) gap doubled — but this is because the gap has narrowed during the lockdown period. Compared to 2019 (the last full year before COVID-19 crisis), Moldova’s CA gap still widened by 41%.

The country’s external deficit thus reached a new all-time record, both in absolute terms and compared to its GDP: the four-quarter CA gap accounted for 12% of the GDP over the same 12-month period ending September 2021.
TURKEY

Turkey. Country of action. The Turkey watcher knows they can hardly take their eye off the place for a split second. And in 2022, such sentiments might apply more than ever. Mired in unprecedented Turkish lira volatility, the nation has entered another phase of escalation in its ongoing collapse in all fields.

It’s well known by now that chaos has beset Turkey’s economy, but how many outside of the country can properly see the chaos that has crept into almost any sphere you can name, from foreign policy to the health system, education system, food security and so on, and on?

The prevailing consensus right now suggests that Turkey is embroiled in a financial and economic crisis, just as it was in August 2018. But this publication is sticking to its contention that the beginnings of the country’s full-blown collapse on all fronts – part of which can be accurately described as a financial and economic depression – can actually be found in the aftermath of the failed coup attempt in July 2016. There has been a nonstop worsening of Turkey’s plight ever since those fraught days when President Recep Tayyip Erdogan declared that he had survived an armed conspiracy to topple him and, emboldened, set about becoming all-powerful.

The last time Turkey saw the type of food and basic goods shortages that are in evidence today was at the end of the 1970s. It was a time when many people died in clashes between the right and left. The PKK, a Kurdish terrorist organisation, arose on that fertile ground. The chaos paved the way for the 1980 military coup.

Turkey rarely enjoys a “bloodless” year, but 2022 has to be marked out as a candidate that will claim an unmissably tragic page in history when it comes to violence.

The only hope for the country is that the Erdogan administration will chance its arm in a snap poll. Ever since the regime lost the Istanbul mayoral election, plus a rerun, in 2019, we have, rather than posing the question of whether Erdogan will lose the next parliamentary and presidential elections, pondered whether any election will be held.

The election does not need to be “fair”. Erdogan will lose any election.

In this most positive case, Turkish assets, led by the lira, would see a sharp rally. It would begin as soon as the market became convinced that Erdogan would have to hand over the reins of power. Turkey would then fall into another “hot money trap”, as all “semi-colonies” do. An actual recovery, which could be described as at least returning to the 2015 settings, would require, at a minimum, five years of uninterrupted healing, with the programme to cover each and every corner of life.

It should be noted that, in the post-Erdogan period, any government, democratic or undemocratic, would have to politically and economically surrender to an International Monetary Fund (IMF) programme. And past experience with IMF programmes shows that political ructions would be in store.

Turkey still has access to borrowing on the global markets – though each instance of borrowing at the required high costs brings the country closer to the ultimate end, namely the IMF programme.

A new version of the ruling Justice and Development Party (AKP), working with the IMF, is the likeliest potential major political change you might see on the road ahead.

The IMF, of course, is far from a font of all wisdom. Among the demands the Fund made with its last standby programme for Turkey, signed in 2001, was a limiting of sugar beet production. Starch-based sugar consumption subsequently boomed. Currently, there are more than 10mn diabetic patients in the country.

Istanbul Mayor Ekrem Imamoglu could be a good candidate for implementing an IMF programme. He is flexible and populist. Deva Party chair Ali Babacan, a former Erdogan ally who was among those who implemented the 2001 programme, anticipates a place at the top table for himself.

The scenario could in a certain sense be seen as identical to what was seen in 2002. Back then, the serving Istanbul mayor Erdogan, was under pressure from the laicist military “tutelage” regime. In the present-day situation, he would be replaced by Istanbul mayor Imamoglu, who is under pressure from Erdogan’s Islamofascist regime. “Moderate Islam” would be replaced by “moderate secularism”.

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UZBEKISTAN

Executive summary
Officials are working on taking Uzbekistan’s “opening up” policy, initiated by President Shavkat Mirziyoyev in late 2016, to the next level.

Mirziyoyev won a fresh mandate in the October 2021 presidential election, securing a landslide victory. With the country hoping a complete recovery from the effects of the coronavirus pandemic is now on the horizon, the Mirziyoyev administration knows there will be no time to waste in delivering gains delayed by the COVID-19 crisis.

However, events in Kazakhstan at the start of the new year may give officials pause for thought. The unrest seen across the neighbouring country might cause Tashkent to take stock of just how fast, and in what fashion, it can proceed in delivering more democratic and economic rights.

Uzbekistan will keep a wary eye on Afghanistan, while maintaining friendly relations with the country’s new Taliban regime in the hope that its neighbour can achieve enough stability to become a crucial element of Tashkent’s ambitions to expand trade with countries across South Asia. An Afghanistan slipping into an economic and humanitarian catastrophe would be somewhat alarming for the Uzbeks, especially from the security point of view. Tashkent has made several carefully elaborated calls to the West to do more to help the Afghans find their way to a sustainable future.

As the economy regains firepower, with the worst of the coronavirus crisis over, the international financial institutions are predicting growth of around 5.5% to 6% this year.

To improve the balance of payments equation, Tashkent is investing in adding value to production. Uzbekistan’s biggest export item is now textiles. The state is aggressively targeting value-added exports. Raw cotton exports have been banned. Cotton growers are thus forced to invest in textile production.

The introduction of inflation targeting is the main focus of the Central Bank of Uzbekistan (CBU). It is striving to anchor the population’s expectations for price rises, a tough task given the horrible experience with inflation Uzbek had prior to the Mirziyoyev administration.

Every economic transformation needs funding, it goes without saying, but dabbing the brake, Tashkent has limited the total volume of domestic and foreign debt to 60% of GDP.

The banks continue to address their “neverending” lack of liquidity and rather high non-performing loan (NPL) ratios. In August, the LDR (Loan-to-Risk Ratio) for the entire Uzbek banking system hit a record 234%.

Uzbekistan’s commercial banks are expected to release $467mn in eurobonds by the end of 2022.

In energy, there are multiple major renewables projects. The government wants the share of renewable energy in energy generation to hit 25% by 2030. In nuclear, this year might bring the start of construction of the country’s first two plants, with the participation of Russia’s Rosatom.

Retail players, meanwhile, say the supermarket sector in particular is “ready to boom”.

As 2022 unfurls, Uzbekistan, standing on the threshold of rich opportunity, will hope global economic winds don’t blow it off course.

Politics
In geopolitics, the re-elected Mirziyoyev is not expected to move far from the strategy long pursued by his predecessor, the late Islam Karimov, namely “taking the middle road”, rather than siding with major powers in key affairs.

Tashkent is cautiously strengthening relations with the European Union. Uzbekistan and the EU in the coming year will hold events including a meeting of the Uzbekistan-EU Parliamentary Cooperation Committee, the European Union-Central Asia ministerial meeting and an EU-Central Asia tourism forum.

Mirziyoyev’s first official trip after his election victory was to Russia. Vladimir Putin remarked: “Uzbekistan is not just our close neighbour, it is also an ally – this is exactly how we treat Uzbekistan. It is a large regional country with which we are connected in many ways – both historically and today.”

Much of the political situation in Uzbekistan will very much depend on how events further unfold in Afghanistan. The social unrest seen across Kazakhstan at the start of the new year might also give officials pause for thought as to how quickly, and in what fashion, more democratic and economic rights can be delivered.

Uzbekistan’s relations with the Taliban have been assessed by political analysts as friendly, evidenced by a number of bilateral negotiations between official figures.
The Taliban leadership promised “not to shoot a single bullet” towards its neighbour. Tashkent is proving helpful in the Taliban’s appeal for the unlocking of Afghan capital frozen abroad to help ward off an economic and humanitarian crisis, though Tashkent’s voice is only one of many in these matters. Uzbekistan clearly doesn’t want to see Afghanistan, on its doorstep, sliding into catastrophe and chaos. And a stable Afghanistan is vital to Uzbekistan’s hopes to build up trade and investment with South Asia.

One political event scheduled to take place in Uzbekistan in the coming year is a summit of the Organisation of Turkic States. The country will also host the regular meeting of the military department heads of the Shanghai Cooperation Organization (SCO) states.

**Macro economy**

Uzbekistan’s macroeconomic development in 2022 should be founded on gradual improvements in external and internal indicators, as long as no significant external risks come to pass. The US Federal Reserves battle with inflation could potentially have negative ramifications for emerging economies worldwide should it not go well.

If the pandemic is successfully beaten back, long-term restrictions on the migration of human resources and cross-border movement will not be introduced.

**GDP growth**

Before the pandemic hit, Uzbekistan’s GDP was rising at a rate of more than 6% a year. But in 2020 growth fell to a mere 1.7%. The bounceback in 2021 brought 6.9% in the first nine months, according to the Central Bank of Uzbekistan (CBU).

As the economy returns to health, the international financial institutions (IFIs) have upped their forecasts for 2022. The International Monetary Fund (IMF) revised its GDP growth outlook for 2022 to 6%. The World Bank is predicting 5.6%, while the Asian Development Bank (ADB) is a little more cautious at 5.5%. The highest growth rate is projected by the European Bank for Reconstruction and Development (EBRD). It sees 6%.

**External environment**

Uzbekistan’s foreign trade has expanded significantly since incumbent Shavkat Mirziyoyev took office in 2016. Since the liberation of the FX market in 2017, companies have leapt at the chance to seal their own export deals and trade is flourishing.

According to official data for January-October 2021, Uzbekistan’s foreign trade turnover got back on the rails following the impacts of the first year of the pandemic, reaching $32.7bn, up 8.5% y/y.

Of the total trade volume, exports amounted to $12.4bn, (down 6.7%), while imports surged 20.5% to reach $20.2bn.

Among the 20 major partner countries of Uzbekistan in foreign economic activity, active foreign trade balances were observed with four countries – Afghanistan, Kyrgyzstan, Tajikistan and Turkey.

China remains Uzbekistan’s most important trade partner. However, turnover with the “ancient” counterpart did not in 2021 regain pre-pandemic levels, whereas trade with the other Central Asian republics and Turkey did surpass the levels seen in 2019.

To improve the balance of payments equation, Tashkent is investing in adding value to production. Uzbekistan’s biggest export item is now textiles. That in itself is a reflection of the state’s new policy of aggressively targeting value-added exports. A ban on raw cotton exports has forced cotton growers to invest in textile production.

Accessions into the EU Generalised System of Preferences Plus (GSP+) scheme and its UK analogue (Generalised System of Preferences Enhanced Framework) will yield trade gains in coming years as tariffs are slashed.

If the country finalises its decision to join the World Trade Organisation (WTO), foreign trade figures can be expected to skyrocket.

**Inflation and monetary policy**

The government forecasts that inflation will decline to 10% by the end of 2021, 9% in 2022 and 5% in 2023.

European Bank for Reconstruction and Development (EBRD) economist Eric Livny observed to bne IntelliNews that even 10% was a rather high figure, but such price growth was not an Uzbek phenomenon as, amid the pandemic, inflation had gained momentum worldwide.

Read the full report online.flipbuilder.com/myab/xztc/
Kazakhstan’s Tokayev slates ‘Nazarbayev’ oligarchs in populist attempt to turn page on country’s unrest

bne IntelliNews

Kazakhstan’s President Kassym-Jomart Tokayev, who showed vulnerability when he resorted to inviting in Russian troops to help stamp out a growing uprising, on January 11 attempted to change the narrative with a populist turn in which he hit out at how “oligarchic groups” took root in the country under his predecessor Nursultan Nazarbayev and announced he was setting up a For the People of Kazakhstan national fund that would require contributions from the wealthy and profitable companies.

In a video call with parliament, Tokayev, who became president in 2019, said that under the 29-year-long Nazarbayev presidency, “a group of very profitable companies emerged in the country as well as a group of people wealthy even by international standards”.

“I think it is time they pay their dues to the people of Kazakhstan and help them on a systemic and regular basis,” he added.

Kazakhstan’s financial system, said Tokayev, was dominated by large business groups “based on the principle ‘everything for friends, and laws for everyone else’”.

‘Abandoned their posts’

Tokayev also hit out at security officials, saying that as the unrest grew they abandoned their posts and let protesters capture weapons and classified documents.

Since the unrest was brought under control, Tokayev, backed in his assessment by Russian counterpart Vladimir Putin, has, without any compelling evidence, doubled down on the claim that the violence on the streets and “attempted coup” were very much the work of foreign-trained plotters and “terrorists”. However, in his televised address to lawmakers, the 68-year-old president conceded that the public discontent over income inequality was justified and he wanted associates of Nazarbayev to share their wealth.

Tokayev – who announced that his new government would be led by career public servant Alikhan Smailov and that Russian troops would begin withdrawing from Kazakhstan in two days – also said: “The time has come to give people
what belongs to them, to provide help systemically. The government must look into such companies to define what their contributions to the For Kazakhstan’s People Fund should be.”

The nation’s oligarchs had caused “seriously restricted development of the free market and dented the country’s competitive edge”, Tokayev, a former diplomat and technocrat known for not having become much involved in business during his career, added.

The new prime minister has been ordered by Tokayev to secure “additional revenue” from oil and mineral-rich Kazakhstan’s mining companies and present a government programme for the year within three weeks, Tokayev said. Gasoline producers, he also stated, must pay higher excise duties without introducing price hikes to consumers.

**Poured scorn**

Tokayev also poured scorn on the state-owned Development Bank of Kazakhstan. He told MPs that it “has essentially turned into a personal bank to serve a circle of persons” representing financial, industrial and construction groups. “We know everyone by name,” he said.

Handing out further orders, he told prosecutors and the finance ministry to overhaul the “real mess” in customs services. The state, he complained, was losing tens of billions of tenge in unpaid duties. Some operators, he said, were seen as “untouchable.”

As analysts looked for Tokayev moves that would directly target people around Nazarbayev, the government received orders from the president to shut down operations of Operator ROP, a major disposal and recycling company that many in Kazakhstan say is connected to Nazarbayev’s youngest daughter, Alia Nazarbayeva.

**Not a word**

Nazarbayev, 81, has not said a word in public since the Kazakhstan crisis begun, though his spokesman has claimed he remains in the capital, Nur-Sultan, and wants the country to unite around the Tokayev administration.

“Tokayev’s speech doesn’t change the overall reform direction,” Tom Adshead, director of research at Moscow-based consultancy Macro Advisory, was quoted as saying by Bloomberg, adding: “What he’s looking for is some demonstrative populist measures against elites who made money under Nazarbayev.”

The presidential decree appointing a new government detailed how the interior minister, defence minister and foreign minister have retained their posts, unlike the ministers of information, justice, health, industry, economy, culture, finance and energy who have been replaced.

The Interior Ministry said on January 11 that security forces have so far detained 9,900 people in connection with the unrest.

Fionnuala Ni Aolain, the UN’s special rapporteur on counterterrorism and human rights, said in a statement that Kazakhstan’s overly broad use of the term “terrorism” to describe protesters, civil society activists, human rights defenders, journalists and political parties “appeared aimed at instilling fear and was deeply concerning”.

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**CSTO comes out of the shadows for the first time**

**bne IntelliNews**

Soldiers from the Russian-dominated Collective Security Treaty Organisation (CSTO) are reported to have arrived in Kazakhstan to help defend President Kassym-Jomart Tokayev against violent protests that have shaken his authoritarian regime.

"Russia’s military units of the Airborne forces have joined the CSTO Collective Peacekeeping Forces. Currently, the aircraft of the Russian Aerospace Forces’ military and transport aviation are sending Russian units of the peacekeeping contingent to the Republic of Kazakhstan," a CSTO statement said.

The forces would be engaged in “the protection of important state and military facilities, assistance to the forces of law and order of the Republic of Kazakhstan in stabilising the situation and returning it to the legal order”. Soldiers from the CSTO’s other members – Armenia, Belarus, Kazakhstan, Kyrgyzstan and Tajikistan – are also expected to take part. According to Armenian news reports, 70 soldiers will be sent.

There have already been reports that Russian special forces participated in an operation to retake control of the airport in Almaty that was briefly captured by the protesters on January 5.

As the rioting intensified on January 5, President Tokayev had appealed for military help "to help Kazakhstan overcome this terrorist threat".

For the first time in its 30-year history the CSTO immediately agreed to send “peacekeepers” and the next day troops had already begun arriving.

“In light of the threats to national security and sovereignty to the Republic of Kazakhstan, including from external interference,” the CSTO would send peacekeepers “for a limited period of time with the aim of stabilising and normalising the situation,” wrote Armenian Prime Minister Nikol Pashinyan, the CSTO’s current head, on Facebook. Pashinyan added that there were “dangers threatening Kazakhstan’s national security.
and sovereignty, which have arisen as a result of external intervention”.

The CSTO is intervening under its Article 4 – a counterpart to Nato’s Article 5 on collective defence – which states: “If one of the States Parties is subjected to aggression by any state or group of states, then this will be considered as aggression against all States Parties to this Treaty. In the event of an act of aggression against any of the participating States, all other participating States will provide him with the necessary assistance, including military, and will also provide support at their disposal in exercising the right to collective defence in accordance with Article 51 of the UN Charter.”

Despite Tokayev’s accusations that he is confronting foreign-trained “terrorist gangs”, no credible evidence has so far been presented that Kazakhstan is facing an external threat by a “state or groups of states”, as mandated under Article 4.

Up until now the CSTO has had little to do. Since the founding treaty was signed on May 15, 1992, the most notable moves were the creation of a Collective Rapid Reaction Force (under a 2009 agreement) and peacekeeping forces (under a 2007 agreement).

Some 3,000 soldiers and 600 interior ministry personnel are assigned to the CSTO peacekeeping force. In October 2016, in CSTO also decided to establish a CSTO Crisis Response Centre in Yerevan, Armenia, which was entrusted with helping to organise any crisis response decisions taken by the organisation.

Ironically the first peacekeeping exercise – “Unbreakable Brotherhood 2012” – was actually held in Kazakhstan. “According to the scenario, a crisis situation arises connected with the activity of international extremists and terrorist organisations and conflict between ethnic groups living in the country,” the CSTO said at the time.

CSTO units regularly hold joint exercises – their latest manoeuvres in October were conducted in Tajikistan, Uzbekistan and Kyrgyzstan in the wake of the takeover of Afghanistan by the Taliban – but never before has the CSTO agreed to send military forces and invoke Article 4.

In 2010 when Kyrgyzstan was experiencing huge ethnic unrest, and in Armenia in 2021, when it looked at one point as if Azerbaijan would not just retake its former territory but push into Armenia itself, the CSTO did not respond to requests for help.

In the case of Armenia, the CSTO sat on the request for three months and then dismissed the incursions as “in essence a border incident”. Eventually Armenia was persuaded not to make a formal request under Article 4.

In the current crisis, some analysts have questioned Russia’s ability to respond, as the troops that would normally travel to Central Asia from Russia’s Central Military District have largely been redeployed to the Western Military district near Ukraine. However, at the moment large-scale deployments of troops are unlikely and Russia should be able to spare units such as the paratroopers that have been deployed. Russian media had reported that an aviation regiment in the city of Orenburg, close to the Kazakhstan border, was “on alert to be deployed to Kazakhstan”.

It is to be seen whether CSTO forces will play a frontline role in putting down the unrest, but even the fact that they have been deployed could damage the credibility of both the Tokayev regime and some of the states taking part in the CSTO mission. If the repression turns very bloody, this could rebound on their reputation both at home and abroad.

For Tokayev, the appeal for Russian help goes against long-standing Kazakh interests in trying to restrict Moscow’s influence inside the country, given its sizeable Russian minority and its history of Soviet domination. His government’s allegation that Kazakhstan is facing “armed aggression from terrorist groups trained outside of the country” looks incredible, given that Kazakhstan is surrounded by other authoritarian states, most of them CSTO members.

There have also been reports that Tokayev discussed the crisis in a call with Belarusian President Alexander Lukashenko, another beleaguered dictator. Speculation that the presidents were discussing how to repress demonstrators and potential Belarusian assistance will further damage his credibility.

The CSTO intervention – compared by some outside observers to the Warsaw Pact repression of the 1968 Prague Spring in Czechoslovakia – could also rebound on the governments taking part.

Most obviously, Armenia, one of only two partly free states in the CSTO according to Freedom House, could be severely embarrassed. President Pashinyan is already facing criticism for authorising the military intervention in his new role as the rotating chairman of the CSTO. Ironically, Pashinyan came to power after Armenia’s own protest movement, and in its subsequent war with Azerbaijan, the CSTO refused to come to its aid.
Fugitive banker Ablyazov lays claim to filling opposition vacuum in Kazakhstan as president says forces will shoot-to-kill

bne IntelliNews

Kazakhstan’s authoritarian President Kassym-Jomart Tokayev on January 7 stepped up his efforts to delegitimise the protests that have this week swept the country by reasserting that they have been organised and driven by foreign-backed “criminals”, “bandits” and “terrorists”. He has instructed the country’s security forces to “use lethal force without warning”.

Such has been the lack of democracy in the Central Asian nation throughout its three-decade-long post-Soviet independence that no substantial organised political parties or movements of opposition have taken shape, meaning the many thousands who have come out on the streets during the unrest have lacked leadership and direction. January 7 thus brought another interesting development when self-exiled France-based Mukhtar Ablyazov stepped forward and attempted to fill the vacuum of opposition.

Ablyazov, however, is a hugely controversial figure. A former Kazakh energy minister, he headed one of Kazakhstan’s largest banks, BTA Bank, from 2005 to 2009 and, with refugee status in France, leads the Democratic Choice of Kazakhstan (QDT) party – banned in his homeland – but at the same time he is a fugitive whom Kazakhstan has tried and sentenced in absentia for murder and embezzlement.

In interviews with news agencies, Ablyazov nevertheless made his case, telling AFP: “The temporary government that ousts the regime of Nursultan Nazarbayev [the former Kazakh president who ruled from 1990 until Tokayev took over in 2019] will be led by me for half a year ahead of free elections.”

‘Restored Soviet Union’

Speaking to Reuters, Ablyazov warned that while Kazakhstan was now in geopolitical play, unless the West entered the fray then Russia – which at the invitation of Tokayev has sent troops to help restore order in Kazakhstan – would bring the Central Asian republic to heel in a type of restored Soviet Union.

"If [the West does] not [act] then Kazakhstan will turn into Belarus and [Russian President Vladimir] Putin will methodically impose his programme: the recreation of a structure like the Soviet Union," Ablyazov – who in 2016 faced an extradition request from Russia that was blocked by France’s highest administrative authority as politically motivated – was quoted as saying.

In further remarks reported by AFP, Ablyazov insisted that the regime that has ruled Kazakhstan since the fall of the Soviet Union is nearing its end in a popular revolution. The Russian-led military intervention of five ex-Soviet states requested by Tokayev to help deal with Kazakhstan’s crisis amounted to an “occupation”, he said, and the West should consider sanctions against the Kazakh leadership, with the Kazakh elite known to have “lots of assets” in European capitals like Paris and London.

"I am urging people to organise strikes and block roads to protest their [Russian and other foreign troops] presence in the country," he was also cited as saying, adding: “The more Putin intervenes, the more Kazakhstan will become like Ukraine – an enemy state for Russia.”

Tokayev, meanwhile, was in no mood for compromise. Promising the crackdown on the protests would continue, he said: “Abroad there are calls for the two sides to hold negotiations for a peaceful resolution. What idiocy. What kind of negotiations can you have with criminals? We were dealing with armed and well-prepared bandits, both local and foreign. Bandits and terrorists, who should be destroyed. This will happen in the nearest time.”

No evidence

A problem for Tokayev and Putin is that the troops arriving in Kazakhstan under the Moscow-led Collective Security
Treaty Organization (CSTO) are doing so according to the CSTO principle that its member states can assist one another against foreign aggressors. Tokayev may have referred to “foreign-trained terrorists” and “financially motivated plotters” from abroad, but he has presented no evidence for these allegations. Putin is in these circumstances vulnerable to charges that he has mounted a police action inside Kazakhstan.

The US on January 7 said it was closely monitoring reports of the deployment of outside troops in Kazakhstan and added that it had questions about whether the forces were legitimately invited to the country.

"We have questions about that deployment precisely because Kazakhstan, the government of Kazakhstan... has its own resources, and the government is and has been well fortified," US State Department spokesperson Ned Price said.

RFE/RL on January 7 told how its correspondent interviewed an activist with Kazakhstan’s unregistered Democratic Party who was in a crowd of 200 protesters at Almaty’s Republic Square the previous day when, he said, shortly after sundown a group of soldiers opened fire with live ammunition. Aigerim Tuleuzhanova asserted that those who were fired upon were young, unarmed Kazakh activists.

Attempting to push back on Tokayev's narrative, activists unfurled banners declaring “We are not terrorists!” and “Tokayev: Don't shoot us!” Tuleuzhanova said.

Moving ahead, Tokayev, who has faced claims that he so rapidly turned to the CSTO because he was not confident that the Kazakh armed forces and police force would stay loyal to the regime should the demonstrations intensify, will have difficulties explaining to Kazakhs why Russian – as well as Kyrgyz, Tajik, Belarusian and Armenian – troops are on Kazakh soil.

"Sovereignty is something that the Kazakh population has really fought for over the years and is extremely proud of," Ben Godwin, a political risk consultant with London-based PRISM, who lived in Kazakhstan for seven years, was quoted as saying by the Canadian Broadcasting Corporation (CBC). He added: "The idea of potentially losing sovereignty due to the presence of foreign forces is very disturbing to many within Kazakhstan."

Fake news? Conflicting reports of shooting in Almaty as Russian and Kazakh governments appear to manipulate reporting for own agendas

Soldiers have started a military operation to clear the streets of Kazakhstan’s commercial capital and largest city, threatening to shoot on sight anyone that ventures abroad. Russian state-owned news agencies have broadcast dramatic video of squadrons of soldiers walking down a wide street that they claim is close to Republic Square in the heart of the old capital and shooting machine guns at unseen assailants.

Russia's flagship English-language channel RT reports that dozens are dead, including ten policemen, and that three of those have been “beheaded.”

The problem is that bne IntelliNews’ correspondent in Almaty says that most of the reports are not true, or are at least highly suspect.

Fake news?
Currently it is next to impossible to verify or confirm the many dramatic reports coming out of Almaty. The internet has been shut down. All the independent media outlets and social media apps like the popular Telegram messaging service are not working.

However, Kazakh state media are still releasing information and the Russian state-owned press is also on the ground and broadcasting, including the Kremlin's RT.

Some independent information is coming out of the country and it seems clear that there have indeed been shootings and killings of both Kazakh police and civilians. What is not known is the scale of the casualties and fatalities. bne IntelliNews’ correspondent, reporting by phone, says that there has been violence and fighting but from what he can glean by calling around to people that live at the scenes of the reported violence, the clashes have been on a smaller scale than some of the reports since January 5 have described with estimates of dozens dead.

The Russian media outlet TASS also reported on the soldiers shooting at Republic Square in the heart of Almaty. The news agency released footage of soldiers in an urban setting shooting down a street at unseen opponents – the source of the video that was used by RT.
The RT report went on to say that banks have been robbed and stores looted. The reporter also claimed that at least 10 police officers have been killed and “three were unfortunately beheaded,” a claim that does not seem to have been picked up by other media reporting on the story and is new compared to early reports of eight policemen that died, reported the day before.

*bne IntelliNews’* correspondent in Almaty warns that reports by the official media and Russian state-owned media should be treated with caution, as they have already reported on shootings that *bne IntelliNews’* correspondent can assess as fake news.

“Those reports, I wouldn’t believe them, as in the physical locations where the shooting is reportedly happening, I called people who live there and they say it has been peaceful all day. Nothing is happening,” *bne IntelliNews’* correspondent said in a phone call from Almaty.

Nevertheless, there have been multiple reports and videos that suggest some of the protesters have got access to guns, and other unconfirmed reports on social media show that there has been shooting in the city.

Official reports of around a dozen deaths amongst the police force also seem creditable, even if the reports of beheadings cannot be confirmed at this time. Video has also surfaced from what appears to be from a morgue of almost two dozen civilian corpses.

Mixed message

Another aspect of the reporting coming out of the old Silk Road way station of Almaty is that the Kazakh and Russian media have been contradicting each other on the severity of the crisis.

The context of Kazakh President Kassym-Jomart Tokayev’s call on January 5 for military help from the Collective Security Treaty Organisation (CSTO) to quell the protests may be a decisive factor here. On the one hand, calling in Russian military is politically embarrassing for Tokayev, who already seems keen to play the need for outside help down; on the other hand, the Kremlin is motivated to hype up the violence in the Kazakh city to justify what it has been selling as a peacekeeping mission to save lives and restore order. Some pundits have already been drawing parallels between the Russian military aid as an “intervention” or reminiscent of Prague in 1968, when the Soviet Union sent in tanks to put down the “Prague Spring” demonstrations.

The situation has been further confused by the speed of the changes in the last three days. On the first day Tokayev addressed the nation with a conciliatory tone and concessions. He blamed and sacked the government for the spike in fuel prices that had sparked the first demonstrations. The subsidies were reintroduced and Tokayev announced a package of aid and price caps to try to deal with the core complaints of the protesters.

As it became clear the next day that these concessions were not going to placate the crowds as the demonstration was already morphing into more general anti-government unrest, Tokayev’s line quickly hardened. He began to talk about “hooligans” and then within hours “international organised and funded terrorists” and “financially motivated plotters”.

Tokayev addressed his unrest-gripped Central Asian nation on January 5, vowing a “tough” response to mass protests over a New Year energy price hike. “As president, I am obliged to protect the safety and peace of our citizens, to worry about the integrity of Kazakhstan,” he said in Russian on Kazakh television, adding that he intends “to act as severely as possible”.

That is when he asked the CSTO for help. However, now the Russian soldiers are on the way, and some are already reportedly on the ground, the Kazakh official media is already backing away from its stern stance.

“The official Kazakh media is already reporting things are calming down and things will go back to normal in the next few days. The Russian media are reporting that all hell is breaking loose,” *bne IntelliNews’* correspondent said.

“The Kazakh media are reporting that the CSTO forces will come to protect infrastructure and will mainly be made up of [CSTO member states] Kyrgyz, Armenian and Tajik forces. However, the Russian media are saying the CSTO forces are coming in and are needed to bring peace,” our correspondent continued.

“From the ground it looks like [the] internet shutdown has been done so people don't know what is going on and stay at home, but when you talk to people who actually live there [amid the locations of the unrest] nothing seems to be happening,” *bne IntelliNews’* correspondent reports. “There is a lot of what looks like misinformation. After
January 4 the next wave of protests were muted. The government stepped back and allowed the ransacking to go on but only now they say they are back in control,” he added.

While RT is reporting on widespread vandalism and looting of banks and stores, our correspondent says the only obvious victim is the large Magnit shopping mall in the centre, which has been attacked, but there is no widespread looting.

Another factor at play is that, as bne IntelliNews has reported, Tokayev appears to have opportunistically taken advantage to the crisis to remove the last hold on power of the former Kazakh president Nursultan Nazarbayev. Tokayev took over Nazarbayev’s job as head of the National Security Council, the successor to the Soviet-era KGB, and has replaced key figures in the administration, including the head of the security services, with people loyal to himself.

“Nazarbayev’s name has disappeared from reporting in the last two days; [he] fled the country on January 5 and is now believed to be in Switzerland,” bne IntelliNews’ correspondent says. “Officially Tokayev now holds all the levers of power.”

Blood on the street
Despite all these complications, the protests in Almaty and elsewhere have clearly got out-of-control and there most certainly have been casualties and deaths. Below bne IntelliNews reports on what has been broadcast and shared, but we emphasise that none of the posts or videos released can be verified.

Moreover, we strongly suspect that some or possibly even all of the posts could be fake, as clearly both the Russian and Kazakh authorities have been trying to manipulate the information reaching the public to bring the protests to an end sooner in the case of the Kazakhs by terrorising the population, and to justify sending Russian troops to another country in the case of the Russians.

While information is sketchy, it is clear that there were major clashes between protesters and Kazakh police and in many incidents the protesters outnumbered the police who were not in control of the situation. Many of these reports were posted on social media before the internet was turned off during the afternoon of January 5.

Some 109 people have been hospitalised, according to official news reports, of which almost all were police officers, strongly suggesting that the demonstrators have had the upper hand on the second day of protests.

On January 5 those reports were followed by new reports of deaths amongst the security services. The Kazakh Internal Affairs Ministry says 10 police and national guard troops were killed in clashes with protesters and another 317 injured during unrest in several regions of Kazakhstan, Russian news service RIA reported. These early reports of the 10 dead policemen made no mention of any beheadings.

The social media that was still possible release on January 5 showed copious video of protesters fighting with police and openly smashing and burning police cars and vans.

In another clip a group of about 20 protesters surrounded an officer in full riot gear and wrestled a shotgun from him and walked away with it. Shotguns are standard issue in protests and used for crowd control but usually fire non-lethal birdshot rather than deadly ammunition. During the Belarusian demonstrations in the summer of 2020 there were several confirmed reports of the use of shotguns firing birdshot against protesters.

But the most disturbing video (WARNING: graphic content) to emerge on social media is a clip circulating on Russian Telegram that appears to be shot from inside a morgue, where some 20 body bags are lined up in a small hall that contain what appears to be normal people who are cut and bruised, covered in blood.

Fight for the airport
The one clash that certainly occurred and was confirmed by Tokayev himself was the fight for the airport in Almaty that was briefly taken over by protesters on January 5, until local security troops recaptured it later in the day.

Tokayev referred to the seizure the next day, saying an assault to recapture it was led by Kazakh paratroopers. However, separately there were reports that Russian Spetsnaz participated in, or even carried out, the operation.

RT broadcast a recorded phone message from a Russian at the airport waiting to fly out as the airport was taken over. The passenger said that the staff of the airport suddenly left.

“There are eight of us sitting here, but all the staff is leaving. They have not told us anything and they have not tried to evacuate us,” the man said. Other reports described the same events, in reports that cannot be independently verified.

However, by the end of the day the airport was back in the government’s hands, although no details of how that was achieved or if anyone was hurt in the operation were given.

The airport currently remains closed and no flights are going in or out of any of Kazakhstan’s three main international airports.

Nazarbayev reportedly left Almaty Airport shortly before it fell into the protesters’ hands on January 5 on a private jet, one of the last flights out of the country.

Guns
It also appears highly likely that some of the protesters have armed themselves. More social media footage showed men handing out rifles and machine guns in the last two days, getting ready to fight.

In another incident, there were unconfirmed reports that protesters had stormed a National Security Committee armoury in Almaty and emptied it of arms and ammo. The footage showed men emptying lockers and gun racks of arms, while at least one man had an RPG (rocket-propelled grenade). ●
Kazakhstan upheaval impacts country’s banks, bonds, equities and uranium and oil industries

bne IntelliNews

All of Kazakhstan’s financial organisations including its banks and stock market remained suspended on January 6 amid the country’s social unrest, according to the press secretary of the National Bank of the Republic, Olzhas Ramazanova.

"The Agency of the Republic of Kazakhstan for the Regulation and Development of the Financial Market and the National Bank of Kazakhstan, taking into account the conduct of counterterrorist operations ... and taking into account temporary disruptions in the Internet ... report the temporary suspension of the activities of all financial organisations," Khabar 24 TV channel quoted him as saying.

Ramazanova also said that the measure was aimed at protecting the life and health of employees and clients of financial institutions, although there are reports of inhabitants of the capital Nur-Sultan and largest Kazakh city and commercial capital Almaty – scene of the biggest deadly clashes between protesters and law enforcement and troops during the week’s unrest – going hungry due to the closure of ATMs [Watch video below]. With the internet communications were disconnected and the internet was closed down by the operator Kazakhtelecom.

Sovereign bonds hit
Kazakhstan’s sovereign bonds were hit as the crisis rapidly escalated and Russian paratroopers were dispatched to assist the ex-Soviet state’s regime.

January 6 saw Kazakhstan's 2045 dollar bond, which had its worst day since the peak of the COVID-19 panic in March 2020 on January 5, slide further, falling as much as 1 cent and nearing 20-month lows.

With a solid macroeconomic position Kazakhstan’s debt has been seen as relatively stable. The nation's debt lost 2.9% last year, according to a Bloomberg index tracking sovereign dollar bonds from emerging markets, so obligations have already lost more value in the first days of January than in all of last year.

Kazakh equities fall in London
The protests this week hit Kazakhstan companies listed in London, mostly raw material producers, with the local exchange in Almaty closed.

“From the market perspective, we note the clear impact on local stocks that were hit in London on January 5, led by internet company Kaspi.kz, down c30% yesterday and another 12% on January 6,” Slava Smolyaninov, head of strategy at BSC GM said in a note.

Equity investors were caught out by the Kazakh demonstrations, which came out of nowhere and hit in the middle of Eastern Europe’s extended Christmas and Orthodox New Year holidays that run to January 14.

The leaderless revolution rapidly expanded and morphed from protests down, shops cannot process digital payments and are demanding cash, unavailable due to the offline ATMs. Also closed amid the crisis in Kazakhstan’s were the country’s three main airports, with all flights cancelled on January 6. With a state of emergency in place, entry to the country to foreigners has been temporarily suspended, RIA reported. Earlier in Nur-Sultan, and in Alma-Ata, telephone communications were disconnected and the internet was closed down by the operator Kazakhtelecom.

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The leaderless revolution rapidly expanded and morphed from protests
against a specific issue – rising vehicle fuel prices – to a more general anti-government movement becoming a political protest.

“Apparently, the situation with street violence in Almaty, the financial center of the country, is out of control with military confrontation and numerous casualties,” Smolyaninov said. “Authorities ordered an anti-terrorist operation in Almaty in the evening of January 6 and called for military support from Russia, Belarus and other member states of the Collective Security Treaty Organization [CSTO].”

The instability and call for a Russia-led CSTO military intervention on the eve of key talks with the US and Nato over a new European security deal has been seen by investors as weakening Russian President Vladimir Putin’s hand going into the talks, which makes a quick resolution of tensions less likely. And that hurt Russian equity prices as well.

The Russian market reacted negatively even though Brent was back trading above $80, causing the leading dollar-denominated Russia Trading System (RTS) index to fall further to 1,540, or 20%, from its 1920 peak level seen at the end of October, said Smolyaninov.

Uranium production ‘unaffected’
Kazakhstan’s reputation for stability under Nursultan Nazarbayev, an autocrat who ruled for nearly three decades until 2019 but appears to have left the country amid the turmoil, helped attract hundreds of billions of dollars of foreign investment into its oil and metals industries, such as uranium extraction.

Kazatomprom, the world’s biggest uranium producer, said on January 6 it was operating normally with no impact on production or exports. "Uranium mining is going according to plan there have been no stoppages. The company is fulfilling its export contracts," a Kazatomprom spokesperson was quoted as saying by Reuters.

Uranium prices have, however, soared in recent days amid the unrest in Kazakhstan, which produces more than 40% of the radioactive metal used in nuclear fuel.

Uranium surged almost 8% to $45.25 a pound on Wednesday from $42 Tuesday, according to UxC data.

Given Kazakhstan’s role as the world’s No. 1 uranium supplier, “it’d be like if the Saudis had issues in oil,” Jonathan Hinze, president of UxCo LLC, a leading nuclear fuel market research and analysis firm, was quoted as saying by Bloomberg, adding: “Even if there isn’t a shortage right now, the potential for this to create a shortage is what people now are trading on.”

Oil stoppage
In southwestern Mangistau province, where much of the country’s rich oil reserves are extracted, Chevron confirmed to Sky News on January 5 that it was working to end a stoppage at its Tengizchevroil venture.

On January 6, TheEdgeMarkets reported Reach Energy as announcing that its unit in Kazakhstan might be affected by the country’s state of emergency declaration. In a filing to Bursa Malaysia, Reach Energy noted that the government of Kazakhstan had declared a two-week emergency regime in Almaty and Mangistau province, where Emir-Oil LLP, the company’s sub-subsidiary is located.

Emir-Oil LLP holds the entire subsoil use rights in an 850.3-square-kilometre onshore hydrocarbon exploration and production contracted area in Mangistau province.●

Masimov’s downfall, from the corridors of power to a jail cell

Joanna Lillis for Eurasianet

Karim Masimov, a hitherto political heavyweight who was sometimes tipped as presidential material, has experienced a spectacular downfall as unrest roils Kazakhstan. First, he was fired from his powerful position as security chief, then he was arrested on treason charges. Eurasianet looks back at the career of the banker turned politician turned security hawk turned (alleged) coup conspirator.

Karim Masimov, Kazakhstan’s former security services chief and close ally of former president Nursultan Nazarbayev, was arrested on suspicion of high treason.
Linguist... and spy?
Born in 1965 in a provincial Soviet city that was then called Tselinograd and is now Nur-Sultan, the capital of Kazakhstan, Masimov became an accomplished linguist in the 1980s, studying Arabic in Moscow and Chinese in Beijing. He also did graduate studies in management in Kazakhstan.

When he later became a politician, rumours swirled that he had worked for the KGB at this time, since this type of background was typical for recruits to the Soviet spy agency.

After Kazakhstan gained independence in 1991, Masimov became a representative for his new country in its trade and commercial structures in China and Hong Kong.

Well-connected banker
He worked in banking in the mid-1990s, at a time when many were making fortunes in the new Kazakhstan’s nascent financial sector.

As chairman of the board at Halyk Bank, he made some powerful connections: The bank is owned by Dinara Kulibayeva and her husband Timur, the daughter and son-in-law of Nursultan Nazarbayev, who was president of Kazakhstan from independence until his resignation in 2019.

Political heavyweight
Masimov later became a loyal stalwart in Nazarbayev’s political team, serving variously as minister of transport, minister of the economy and deputy prime minister before becoming prime minister.

He served two stints in that job: from 2007 to 2012 and from 2014 to 2016, working as Nazarbayev’s chief of staff in the interim. As PM, Masimov was generally regarded as affable and open, and sometimes tipped as a future president – though his mixed Kazakh-Uighur ethnic heritage was viewed as a factor that would hold him back in a country where people expected a full-blooded Kazakh as president.

Masimov once forced a media outlet to issue a rebuttal to a report claiming that he was Uighur, on the grounds that his Uighur heritage is on his mother’s side, whereas ethnicity derives from the father by Kazakh tradition. In 2016, Nazarbayev appointed him as security chief, the position in which he was allegedly fomenting treason.

Boogieman
The most abiding image of the mustachioed Masimov in this rollercoaster of a career is of him boogying on down in a trendy nightclub in the capital, then called Astana, before it was renamed after his political mentor Nazarbayev, back in 2008.

“Masimov entered at approximately 11:30 pm, accompanied by Presidential Administration head Kairat Kelimbetov, Astana Mayor Askar Mamin, three middle-aged Kazakh women (presumably their wives) and a security detail,” US diplomats recalled in a Wikileaks cable.

“Although the club offers a VIP area, Masimov chose to sit at a table in full view of all of the club’s patrons.” A US diplomat “lingered close to Masimov’s group and saw several bottles of alcohol on the table,” the cable noted earnestly.

Masimov is then depicted as a bit of an exhibitionist, as he “led his companions on to Chocolat’s dance floor soon after their arrival” and “chose to dance on an empty stage above the dance floor.”
Kazakhstan and Belarusian CSTO peacekeepers spotted wearing blue UN peacekeeping helmets

Dominic Culverwell in Berlin

Kazakh state media caused a stir after it photographs of state security forces wearing blue UN helmets at a checkpoint in Almaty on January 9.

Kazakh President Kassym-Jomart Tokayev called in Collective Security Treaty Organisation (CSTO) peacekeepers from Russia and the other member states to quell violent protests that threatened to topple the government, and blamed international terrorist groups. However, this was not a UN operation nor was the UN approached for help, raising the question of why are the Kazakh troops wearing the trademark UN blue helmets?

Experts quickly pointed out that the soldiers were part of KAZBAT, a peacekeeping military unit in Kazakhstan’s army trained to United Nations standards. However, despite their training, KAZBAT is not authorised to wear UN insignia unless they are on an official UN peacekeeping mission.

In response to online criticism, the Permanent Mission of Kazakhstan to the United Nations released a statement that “measures were taken to prevent the use of any equipment bearing the UN inscription” but the mission failed to explain why the helmets were being used.

And the KAZBAT troops were not alone in using UN emblems. The Belarusian Ministry of Defence published photos showing soldiers of the CSTO mission deployed to Kazakhstan, in Belarus’ first ever foreign mission since the fall of the Soviet Union, wearing UN patches on their sleeves. Following public outcry, the United Nations expressed “concern” over the unauthorised use of its trademark symbols.

The reason for publishing these photos is not clear. However, they may be intended to add legitimacy to President Tokayev’s and Russian President Vladimir Putin’s dubious narrative that Kazakhstan is under attack from international terrorism, and to justify the government’s heavy-handed response.

An estimated 164 people were killed in the protests, with Tokayev blaming the violence on some “20,000 terrorists”, but the government has been unable to produce any evidence to support this claim as all the bodies of those killed have been stolen, the government asserts.

“The terrorists] cunningly broke into the morgue and stole the bodies of the dead comrades, so there may be no evidence”, the Kazakh president said on state TV on January 10 in a bizarre address.

Videos allegedly showing armed militia groups and foreign protesters-for-hire have also been debunked or doubted by experts. Even the reports of protesters killing security forces conflict with one other. Disinformation plagues
Kazakhstan, as the state retains total control over the information flow and most of the independent media outlets are currently shut down.

**Who are the protesters?**

If the protests are not being organised by international terrorists then who, if anyone, is behind the unrest?

The first demonstrations appeared in the western Mangystau region on January 1 after a reform saw fuel prices double overnight and protesters were entirely comprised of disgruntled workers.

Despite the efforts of local authorities to meet demonstrators’ demands, the protests quickly spread across the country and morphed into a more general anti-government protest, fuelled by the frustration of poor, malcontent working-class citizens, tired of the country’s corruption and autocracy.

After thirty years of autocratic rule under the former Kazakh president Nursultan Nazarbeyev, the Kazakh opposition movement has been effectively crushed and plays little role in the country. What unrest there has been is largely driven by socio-economic issues and is largely spontaneous. And during the crises of the last year life has become much harder. Inflation rose to 8.9% in 2021, up from 7.5% in 2020, and as food prices have soared, which make up a much larger share of the poor’s shopping basket, this inflation has disproportionately hurt those at the bottom of the social pyramid. Many Kazakhs have been forced to borrow to make ends meet and the population’s debt load increased in 2020 by 12.3%, according to a report by the US think-tank Carnegie Endowment for International Peace in Moscow.

Moreover, thanks in part to the pandemic and little financial support from the government, unemployment rose by 12% last year, particularly affecting young, male, internal migrants from poorer regions. On top of all that, the cost of living in Kazakhstan’s remote western regions is higher than in the more populated south-eastern regions as the price of most of the consumer goods is driven up by the high cost of transport, making Mangystau more prone to protests than the rest of the country.

Kazakhstan’s largest city, Almaty, quickly became the epicentre of last week’s violence. *bne IntelliNews’* correspondent in Almaty reports that the most active centre of protests was in the working-class districts in the southern part of the city. Tensions have also been fuelled by rising youth unemployment after the population nearly doubled in the last 20 years, partly due to the number of internal migrants seeking work. Almaty’s crime rate has risen alongside the population growth, with registered crimes quadrupling between 2007-2017, according to Carnegie.

Although most of the city’s protesters were peaceful, there were reports of fights between security forces and the crowds. With so many young, frustrated men, the radical escalation of the protests was likely down to “the sheer number of angry young men with little to lose”, rather than any foreign influence, Carnegie reports.

A government investigation is underway to determine the cause of the riots, the results of which will no doubt be in their favour. In the meantime, Tokayev promises a “reform plan” and solutions to the country’s “social and economic problems”. However, the outcome of the protests will likely be further persecution and restrictions. In addition to the “terrorists”, Tokayev has his sights set on “human rights defenders”, “activists”, and the “so-called free media”, all of whom he calls “instigators” in the protests.
The Vienna Institute for International Economic Studies (wiiw) has hiked its 2021 CEE growth forecast but lowered its predictions for 2022 and 2023 as the region’s economies slow down amid the withdrawal of coronavirus (COVID-19) pandemic aid.

In its winter forecast released on January 26, the wiiw raised its 2021 forecast of average growth in the region from the 5.4% forecast in October to 5.7%, but has lowered this year’s forecasts from 3.7% to 3.2%. The 2023 forecast has been cut to 3.0 from 3.5%, while the wiww predicts 3.1% growth in 2024. The institute names inflation, the Ukraine crisis and COVID-19 as posing downside risks.

The Vienna Institute explained the expected 2.5 percentage point slowdown in growth this year on the performance of the region’s biggest economies, Russia and Turkey. Turkish growth is anticipated to slow to 3.5% this year, from a forecast 9.5% in 2021, as the country’s economic boom collapses, bringing with it a sharp depreciation in the lira and soaring inflation.

For Russia, GDP growth is forecast to slow to 2% this year from 4.5% last year, and to decline further to 1.5% in 2023, all on the assumption that tougher sanctions will be imposed over the Kremlin’s sabre-rattling in the crisis over Ukraine.

The wiiw noted, however, that Russia’s resilience to sanctions had improved. “The scope for forcing Russia to change its
behaviour over Ukraine using economic sanctions is limited,” pointed out Richard Grievson, deputy director of wiwi.

Conservative monetary and fiscal policies have enabled Russia to build up substantial foreign exchange reserves of $630bn. Gross foreign exchange reserves, including gold, accounted for about 40% of Russia’s GDP in November. External debt is low, and there has also been a reduction in exposure to the US dollar in government bonds.

The wiwi now forecasts average growth in 2022 in the V4 states of Central Europe at 4.4%, followed by 4.4% in 2023. For 2022, it now views the growth prospects of Bulgaria (3.8%), Czechia (4.0%), Serbia (4.9%) and North Macedonia (3.5%) in a somewhat more positive light. Meanwhile, Belarus (1.0%), Bosnia and Herzegovina (2.5%) and Slovakia (3.9%) have experienced a downward revision.

The wiwi says high inflation is the biggest risk to economic recovery in the CESEE region – ranking ahead of both the conflict with Russia and the COVID-19 pandemic.

After 8.7% inflation last year, it expects a weighted average of 10.3% in CESEE this year – and in Turkey as much as 26.2%. However, the inflation rate in the Visegrad countries of Poland, Czechia, Slovakia and Hungary should average 5.2%.

It predicts that price increases will level off by the middle of the year because the worst distortions on the supply side – the problems with international supply chains – should have been eased by then, while the high energy prices are also unlikely to persist.

The wiwi report, however, warns that inflation risks becoming entrenched in Eastern Europe if it leads to a wage-cost spiral. “If it does, we are in for a protracted period of inflation that will be significantly higher than most states in Eastern Europe have experienced since 2008,” said Grievson.

Spending on energy and food accounts for a much higher share of total spending than it does in Western Europe. As a consequence, the governments of Hungary, Serbia and North Macedonia have already introduced price controls on food, not least for reasons of domestic political stability. Meanwhile, Poland and Romania are discussing a similar move.

Overview 2020–2021 and Outlook 2022–2024

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1) *w* estimates. 2) Current account data include transactions within the region (sum over individual countries). 3) Forecasts estimated by wiwi.
Emerging Europe M&A soars by 55% to €94bn in 2021

Mergers and acquisitions in Central and Eastern Europe recovered to pre-pandemic levels in 2021, rising by 18.2% in terms of volume and by 55.1% in terms of value, according to the Emerging Europe M&A Report 2021 by law firm CMS and information platform EMIS published on January 27.

CMS called 2021 “a year of rebound and recovery for dealmakers in emerging Europe”, after 2020 was blighted by the pandemic. In 2020 deal value had fallen for the third year in a row and there had been the lowest number of deals in the 10 years CMS had been publishing the report.

Last year, by contrast, with 2,015 transactions, deal numbers exceeded those of 2019 (1,958), while overall deal value reach its highest level since 2013 at €94.27bn as low interest rates and big cash piles pushed up valuations. The region (which for the report includes Turkey) has now experienced five consecutive quarters with deal values well over €20bn.

“M&A activity in emerging Europe experienced a resurgence in 2021, with buyers and sellers appearing to recover their confidence at the prospect of the pandemic being brought under control,” said Horea Popescu, head of CMS’s CEE Corporate M&A practice.

Looking ahead, Radivoje Petrikic of the CEE Corporate Practice said: “Although uncertainty about the impact of new variants and the prospect of economic fallout from higher inflation has led to a more cautious end to the year, our findings show that dealmaker confidence has largely been restored. In 2021, the main drivers of deals were long-term underlying trends, such as digitalisation, and with the pace of change and shift to digital continuing to accelerate, the fundamentals for an active dealmaking market remain firmly in place.”

The two biggest deals last year were US Norton Lifelock’s €7.34bn takeover of Czech anti-virus software company Avast Software, and Russian Sibur Holding’s €6.08bn acquisition of petrochemical company Taif Group.

It was a record year for IPOs, as the number of listings surged to 116 (up from 26) and values jumped to €13.47bn (up from €4.79bn). Six out of the 10 largest IPOs happened on international exchanges, where they raised nearly €7bn, including the €3.22bn listing of Poland’s parcel locker company InPost in Amsterdam and the €1.48bn listing of Russian retailer Fix Price Group on the LSE. At the regional exchanges the largest listings were those of Pepco Group (€825mn) and Huuuge Games (€367mn) in Warsaw, as well as United Medical Group (€423mn) in Russia.

Telecoms and IT accounted for five of the 10 biggest deals of the year and registered the highest overall deal value at €23.4bn. Transaction numbers rose to 450 (up from 333). Significant Telecoms deals included the sales of Polkomtel Infrastruktura and UPC Polska in Poland, and the sales of Ceské Radiokomunikace and a 30% stake in CETIN in the Czech Republic.

Notable software deals included the €7.3bn sale of Avast Software in the Czech Republic and the €1.6bn purchase of game developer Nexters Global by Kismet, both arising in Russia.

Real Estate and Construction was the second-busiest sector, experiencing 340 deals (up from 310) and a 3.8% rise in deal value to €9.83bn.

Manufacturing was the third-busiest sector with 253 transactions (up from 236) and second by value at €18.26bn.

Mining, Oil and Gas was the third-largest sector by value at €10.59bn, though it was one of the few sectors where deal numbers declined (down to 105 from 124).

Growing investor interest in climate action helped drive up the overall number of

Private equity

Deals by value and volume

www.bne.eu
energy and utility deals to 122 (from 73). The renewables sub-sector saw particularly impressive growth in both deal activity and value, numbering 81 deals (up from 44) and a fourfold increase in value.

In terms of countries, Russia saw M&A activity bounce back, with transactions up by 15.8% to 609 and deal values up by 51.2% to €45.38bn. Values were the highest since 2013, lifted by megadeals such as the €6bn merger of petrochemical groups Taif and Sibur.

Deal numbers recovered strongly in Ukraine, up 57.1% to 143, and deal values more than doubled to €1.72bn, as four deals came in above €100m.

In Poland deal volumes were down 4.3% at 270, but deal values, up 2.3% at €11.93bn, were at the highest level in the past decade. The biggest deal was the €2.5bn acquisition of insurer Aviva Poland by Allianz of Germany. Real estate was the busiest sector by volume, accounting for a quarter of deals, while Telecoms and IT was the largest by value, including the €1.56bn purchase of Polkomtel Infrastruktura by Cellnex of Spain and the €1.52bn purchase of UPC Polska by Iliad of France.

In Czechia, despite deal volumes easing back 7.6% to 110, the value of deals reached an all-time high of €13.37bn thanks to the €7.3bn purchase of Avast Software by Norton Lifelock of the US.

In Turkey volumes increased by 27.2% to 234 deals, in line with pre-coronavirus (COVID-19) levels, while values dipped by 12.3% to €6.89bn, still above 2019 levels. The largest deal was the €1.28bn fundraising by e-commerce platform Trendyol.com from an international consortium including Softbank.

Deal flow in Romania hit a new record at 195, an increase of 43.4%, while value slipped 9.6% to €2.37bn, with the largest deal Romgaz’s €916m acquisition of the Neptun Deep Block.

In Croatia records were broken as deals hit 69, up 60.5%, and value rocketed by 387% to €1.86bn.

The United States was the most active foreign country investor. US deal numbers rose to a decade high of 154 (up from 94) and values more than doubled to reach a record high of €9.17bn.

By deal activity, the top three European investors were the UK (106 deals), Germany (81 deals) and France (54 deals). By deal value the top three were Germany (€3.13bn), with the UK (€2.08bn) and France (€1.91bn) following in second and third place respectively.

The UAE moved up the foreign investor ranking to secure tenth position for its deal numbers, the highest outside the US and Europe.

Cross-border M&A remained buoyant, with deal numbers up 28.9% (985 deals) and values up 59.8% (€56bn). This was well ahead of domestic deal values of €38.3bn (up 48.1%), with deal numbers still slightly higher at 1,030 (up 9.5%).

Russia was the largest single investor country overall, with 564 deals worth €37.3bn – almost all (96%) of these being domestic transactions.

Emerging Europe private equity activity rose further with deal numbers at an all-time high (399) – representing one fifth of overall deal volume – and values up 18% to €23.75bn.

Among the venture capital deals, there were a record 308 deals, up a record 74%, with value more than doubling to €7.7bn. Russia was the leading destination by volume with 74 deals, while Turkey was the top VC investment destination in terms of total value invested at €2.5bn, followed by the Czech Republic at €1.5bn.

The Telecoms & IT sector was unsurprisingly the most active by VC deal count with 186 deals, or 60% of all activity. It also led in terms of value, with deals worth €2.7bn, ahead of Wholesale & Retail, which had deals worth €2.66bn. ●

“IIn terms of countries, Russia saw M&A activity bounce back, with transactions up by 15.8% to 609 and deal values up by 51.2% to €45.38bn”

2021 dealmaking in emerging Europe at a glance

Deals by value and volume

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Giedrius Sniukas of the Bank of Lithuania says the money laundering scandals were an “alarm call”. The central bank is now going to pay closer attention to fintech, he says, given the expected further expansion of the sector and the coming into effect of a unified EU regulatory measure in November 2021. The Bank of Lithuania says that the quality, not quantity, of fintechs will now be its main concern.

Lithuania is already the EU leader in the number of fintechs, partly because it only requires a minimum capital of €1mn. It now hosts over 230 fintechs – half of them Lithuanian-owned. Most of these are small firms focused on payments, financial software, digital banking and lending activities. Big foreign names with significant operations include Revolut, the London-based neobank, for which Lithuania is its EU base.

The scandal sparked international criticism of Lithuania’s allegedly ‘light touch’ regulation, though the central bank pointed out that it had rejected more than 100 applications for a fintech licence in 2020.

Lithuania looks for quality, not quantity in fintech

Linas Jegelevicius in Vilnius

Fintechs have been popping up in Lithuania like mushrooms after warm summer rain. But now the country – one of the biggest fintech hubs in Central and Eastern Europe – is pushing on the brake pedal.

The central bank is implementing tighter standards following a major international scandal involving a Lithuanian fintech. German prosecutors allege that UAB Finolita Unio, a fintech registered in Lithuania’s capital Vilnius, was used to steal more than €100mn from Wirecard in March 2020 just before the German payments company collapsed.

The Bank of Lithuania, under new broom Gediminas Simkus, stripped Finolita of its licence in June 2021, saying it had treated anti-money-laundering and counter-terrorist financing rules “irresponsibly”, and had failed to assess the risks of its customers.

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Among more general measures, the central bank has already tightened borrowing rules and in 2020 it established the public-private Centre of Excellence for Anti-Money Laundering. It says it is now forcing new fintech entrants to meet higher quality standards. The bank has set out its expectations for electronic money and payment institutions in a letter to fintech managers.

“The Bank of Lithuania will pay particular attention to strengthening the compliance culture, i.e. how financial market participants comply with the requirements for the prevention of money laundering and terrorist financing, equity capital, protection of client funds and quality of services, and seek greater personal responsibility of managers,” says Simonas Krepsta, a board member at the Bank of Lithuania.

Following a boom in new entrants over the past few years, there was a slight correction last year as the new tighter rules came into effect. In 2021, 28 licences were granted to new fintech market players, while eight lost their licences, two over money laundering concerns. This compares with 35 licences granted in 2020 and 28 in 2019. By the end of 2020 (the latest figures available) the bank says there were 230 operating fintechs in Lithuania. It says it is currently assessing 40 applicants for licences.

Balancing growth with compliance

The central bank says it wants to balance growth with compliance. “The most important thing for us is for market participants to match business growth with compliance,” says Sniukas.

But market players worry that the new tighter rules could remove Lithuania’s competitive advantage and restrict its future growth.

Airidas Puodziunas, general manager at Contis, a B2B banking and payment solutions provider, told bne IntelliNews: “Lithuania regulators have to get the balance right between heavy-handed regulation that protects customers and the country at large, and a lighter touch that will allow a competitive fintech environment to thrive.”

Lithuania has two sandboxes that enable fintech companies to test their innovative solutions in a supervised and regulated environment before introducing them to the rest of Europe, and then to the rest of the world.
Puodziunas says that by adopting the new quality standards, Lithuania is in effect creating a “new type of sandbox” where regulation itself will be tested. “Not one where products are necessarily tested against regulation, but one where regulation itself is tested against the needs of a thriving market. The prize for sticking to internationalist principles are substantial,” Puodziunas says.

“The government is now looking ahead to ensure the sector’s future. Manauskas, Vice-Minister of Finance, told bne IntelliNews that the ministry has brought together a team of experts consisting of representatives of state institutions and market participants to prepare recommendations for the guidelines on fintech sector development in Lithuania in 2022-2027.

“The recommendations will aim to identify the measures needed to further develop the sector, increase the use of digital financial services, promote the creation and use of innovation as well as strengthen risk management. The government has a clear political will to maintain and strengthen Lithuania’s position as a regional fintech hub. The further development of the sector, both in terms of quantity and quality, requires effective co-operation between public authorities and an open dialogue with market participants. We are on the right track, and it is important to move forward in a focused and measured way,” he says.

Vibrant ecosystem
Market players say that, even with tighter regulation, Lithuania still has many advantages for fintechs. Lithuania became a fintech hub because of the way the sector’s actors have come together to build it up, from the central bank as an innovative regulator with a streamlined application process, the government, which understands the value of adapting fast, through to industry associations building a close-knit community.

Lithuania has one of the highest per capita ratios of ICT specialists in the world and has streamlined Blue Card and Startup visa procedures for non-EU talent. It also has world-class ICT infrastructure with fast broadband speeds.

This has helped build a vibrant fintech ecosystem, which is strongly supported by hubs, accelerators, venture capital funds, and fintech service providers. Some 4,000 people are now thought to work in the sector.

The amount of payment transactions carried out by electronic money and payment institutions in the first half of 2021 was almost six times the same period in 2020 at €122bn. Companies received €208mn in income from licensed activities – an increase of €168mn compared to the first half of 2020.

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Crypto challenge
One of the biggest future challenges for fintech regulation is how to cope with the crypto currency boom. Rising valuations for bitcoin and other crypto currencies are attracting retail investors, who need protection because of the extreme price volatility. At the same time crypto currencies are often still abused for fraud and money laundering.

Raymond Hsu, crypto currency wealth management platform Cabital’s co-founder & chief executive officer, told bne IntelliNews that Central and Eastern European countries have some of the most vibrant fintech hubs in emerging Europe. According to him, the region in the last few years has “really embraced” innovation and has nurtured talent, and all of this is allowing them to support the growth of their fast-growing fintech industry.

As the capital and economic centre of Lithuania, Vilnius, he says, was a natural choice for the crypto community, as it recognises that it would be comparatively easier to hire experienced employees who would most likely be based in the financial service businesses located there.

“Lithuania was selected after an extensive feasibility study for a few key reasons, the first being the country’s rule of law and clear regulatory requirements for crypto currency businesses like ours. Having clear laws and regulations in English helped a great deal in allowing the company’s international team to clearly understand the requirements needed to incorporate the company and to register its business with the relevant authorities.”

“Second, Lithuania’s business friendliness to fintech startups like ours was another key factor. We noted that the country’s banking regulator, the Bank of Lithuania, has a comprehensive newcomer programme catered to fintech startups, which would be ideal for our eventual business expansion into other areas of financial services such as fiat currency payment capabilities,” Cabital’s CEO said.

Hsu said that although the Bank of Lithuania has a strong track record of supporting the payment industry, its new team will need “some time to clarify their stance” on the emerging crypto currency industry. “Regulation and compliance demands will become more complicated as the adoption of crypto currency accelerates,” Hsu emphasised.

“I believe that they will soon get back on track to embrace and regulate the crypto currency industry in a fair and sustainable way,” he said, adding.

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Spread of Omicron pushes coronavirus infections to all-time highs in parts of Southeast Europe

Denitsa Koseva in Sofia

The Omicron variant of the coronavirus (COVID-19) is spreading across Southeast Europe where the number of new cases is rising sharply, reaching all-time highs in some countries. The situation is worsened by the low vaccination rate.

In Bulgaria, the authorities reported 6,766 new cases of coronavirus in 24 hours on January 6, almost reaching the peak of the previous wave of the pandemic in the autumn. A day earlier, the new cases stood at 6,252. The figures were significantly higher compared to the previous days when new cases were around or below 2,000 per day.

The country's health ministry noted that more than 70% of all new cases were among people who have not been vaccinated against coronavirus.

Despite the surging numbers, so far the authorities do not intend to tighten restrictions within the country and are trying to persuade people to vaccinate. However, the restrictions for entry in the country are being tightened as of January 7. People coming from countries that are in the red COVID-19 zone can enter Bulgaria if they have a green...
coronavirus certificate proving they have been fully vaccinated or recovered from the virus, as well as a negative test for coronavirus carried out within 72 hours before entry.

Meanwhile, Bulgaria's ruling coalition has split over an initiative to introduce mandatory green coronavirus certificates for people entering parliament. On January 5, parliament’s committee decided that the document will become mandatory after voting by MPs. However, a day later, Toshko Jordanov, the head of the parliamentary group of There Are Such People (ITN) – a member of the ruling coalition – warned that his party would not back that.

In Croatia, the number of new cases posted a new record high on January 6, going beyond 9,000 in 24 hours, after passing the 8,500 mark a day earlier. The cases were particularly high in Split-Dalmatia county, followed by the capital Zagreb. One fifth of the cases are in these two areas.

Prime Minister Andrej Plenkovic has commented that most likely the Omicron strain is widespread in the country already and urged unvaccinated people to get the jab as soon as possible and for those who have been vaccinated to receive a booster dose.

So far, 63% of the adult population has received two doses, while 543,000 people have had boosters.

In Montenegro, the number of new cases has also surged. According to data from the Institute for Public Health, more than 2,800 new cases were registered on January 5 in the country of just over 620,000 people. As the country is celebrating Orthodox Christmas, it is likely that the number of registered new cases will be lower at the end of the week due to the lower number of tests.

In an attempt to contain the spread of the virus, the government tightened the restrictions for entry in the country as of beginning of January. People can enter Montenegro if they have a coronavirus certificate proving they have been fully vaccinated or recovered from the virus, as well as a negative test for coronavirus carried out within 72 hours before entry.

Top EU court says Bulgaria must issue ID to baby girl with two mothers

Denitsa Koseva in Sofia

The European Union’s top court has ruled that Bulgaria must issue an identity document to a baby girl born in Spain to a same-sex couple from Bulgaria and Gibraltar in a ruling seen as historic by local LGBT organisations.

The ruling of the European Court of Justice (ECJ) concerns a married couple in which both women are recognised as mothers on their child’s birth certificate, issued in Spain where they live. However, Bulgaria does not recognise same-sex marriage and refused to name both as mothers in a national birth certificate, which is needed for the baby to get a Bulgarian – and hence an EU – identity document.

“Since [the baby girl] S.D.K.A. has Bulgarian nationality, the Bulgarian authorities are required to issue to her a Bulgarian identity card or passport stating her surname as it appears on the birth certificate drawn up by the Spanish authorities, regardless of whether a new birth certificate is drawn up,” the court ruled.

It added that such a document, whether alone or accompanied by a document issued by the host member state, which is Spain, must enable the child to exercise the right of free movement with each of her two mothers.

The court also noted that each EU citizen has the right to lead a normal family life.

“Since the Spanish authorities have lawfully established that there is a parent-child relationship, biological or legal, between S.D.K.A. and her two parents, attested in the birth certificate issued in respect of the child, V.M.A. and K.D.K. must, pursuant to Article 21 TFEU and Directive 2004/38, be recognised by all Member States as having the right, as parents of a Union citizen who is a minor and of whom they are the primary carers, to accompany that child when she is exercising her rights,” the court said.

In April, the Court of Justice of the European Union also ruled that Bulgaria should issue ID papers to the baby girl and recognise the parenting rights of her two mothers.
certificate proving that they have been fully vaccinated with one or two doses no more than six months ago or if they have recovered from coronavirus within the past six months. They will be obliged to also present a negative test for coronavirus along with the certificate.

Albania reported a record 1,236 cases on January 5, only to surpass that level with an increase to 1,648 on January 6. A total of 3,829 people tested positive for coronavirus in Slovenia on January 6, an increase of 124% on the same day a week ago, data from the National Institute of Public Health shows.

550 people are being treated in hospitals, 161 of them in intensive care. The youngest patient in an intensive care unit is just 21 years old. Five more people died of COVID-19 on January 5. The National Institute of Public Health estimates that there are currently 25,752 active cases in the country. The number of confirmed cases per 100,000 population in the last 14 days is 1,213, and the average number of confirmed cases in the last seven days is 2,361, according to National Institute data. Additional reporting from Eldar Dizdarevic in Sarajevo.

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**Erdogan follows latest ‘unbelievable’ rate cut with 50% boost to Turkey’s minimum wage**

bne IntelliNews

Turkey’s president, Recep Tayyip Erdogan, on December 16 piled on the pain for Turks suffering from the collapse of the Turkish lira with another rate cut before offering some relief with the announcement that the minimum wage would be lifted by 50% to maintain its US dollar value.

Analysts, however, were quick to serve warning that the minimum wage increase to Turkish lira (TRY) 4,250 ($271) from 2022 would further drive up rampant inflation. Marek Drimal at Societe Generale, for instance, said it would “fuel inflation pressures further, together with the cumulative impact of the lira’s weakness”.

The dollar value of the 2021 minimum wage of TRY 2,825 per month has sunk to $185 from $380 since the start of the year in line with the halving of the value of the lira. And there are fears that hyperinflation has set in in Turkey. Though official inflation is running at 21%, independent analysis led by Turkish academics at ENAG calculates that it has reached at least 60% and continues to shoot up.

Usual defiant self

Erdogan, widely seen as running Turkey’s monetary policy from the palace, was his usual defiant self after waving through a 100 bp cut – to add to 400 bp of cuts made since September – in the central bank’s policy rate to 14%, announcing the improved minimum wage and promising unspecified measures to ensure lira stability in the coming days. The latest rate cut in the face of surging inflation sent the TRY to yet another all-time low against the USD.

Erdogan has asserted that he is fighting an “economic war of independence” to boost domestic industry and ensure Turkey cannot be bashed by the global markets, but the country is hugely reliant on foreign capital, thus analysts generally see him as pursuing a crazy economic experiment, bidding to build short-term popularity with a credit-fuelled economy ahead of elections that must be held by June 2023. The central bank has signalled that it may now pause monetary easing until at least the second quarter but with the mercurial strongman in charge no-one can really know where policy goes from here.

‘Expected, but still unbelievable’

Ahead of the rate cut, the markets were crying out for a change of course, but were resigned to the latest decrease being pursued nonetheless. The rate cut was “as expected, but still unbelievable,” John Hardy, head of FX strategy at Saxo Bank, commented.

"Analysts were quick to serve warning that the minimum wage increase to Turkish lira (TRY) 4,250 ($271) from 2022 would further drive up rampant inflation"
Tolerance for lira pain

At Scope Ratings, Dennis Shen noted that "the central bank’s tolerance for lira pain certainly appears much higher this go around with Erdogan now more or less fully in charge of rates policy.

"The only thing is that even if destabilising lira devaluation is somehow being fully justified away as being good for correction of the current account and raising exports, now that the lira crisis is starting to have an effect on dampening growth conditions – whether such weakening economic growth might force Erdogan to change course ahead of elections by 2023?"

"If so, any ‘change of course’, however, may not mean a rate hike immediately even if the central bank pauses rate cuts at least over the near future, instead potentially meaning capital controls, more FX swaps with domestic banks and friendly allies, and use of reserves to support lira should lira sell-off pressures continue."

"Considering inflation in Turkey will rise to 35% and more mid-next year... we think these measures will not be enough and the bank will have to raise the policy rate in the not-so-distant future"

Ipek Ozkardeskaya at SwissQuote Bank, said he now expected the USD/TRY to end the year within the 17-19 band.

Haluuk Burumcekci at Burumcekci Consulting said in a note: "[The central bank] at least giving the signal that it won’t lower interest rates until March is a limited positive development for the Turkish lira... The central bank will most likely try and navigate this period by using macroprudential tools, primarily required reserves, and by resorting to direct forex sales in the market at times. In other words, without raising interest rates."

He added: "Considering inflation in Turkey will rise to 35% and more mid-next year due to the recent lira outlook, the possible minimum wage hike, significantly deteriorating inflation expectations and the global inflation backdrop we think these measures will not be enough and the bank will have to raise the policy rate in the not-so-distant future."
Police stepped in to disperse an angry crowd of supporters of former Democratic Party leader Sali Berisha outside the headquarters of Albania’s main opposition party on January 8.

Berisha has been seeking to oust the party’s current leader Lulzim Basha, who expelled him from the Democrats’ parliamentary group after Berisha was sanctioned by the US, which accused him of involvement in “significant corruption”.

Berisha supporters gathered outside the Democrats’ headquarters in Tirana at around 10am on January 8. Around an hour later, several hundred people forced their way through the barriers outside the building, smashed windows and forced their way inside.

Footage from outside the Democratic Party headquarters shows protesters repeatedly smashing a sledgehammer against the doors. Others propped up ladders to scale the walls of the building.

MPs loyal to Basha inside the building called the police saying they feared for their lives. Local media reported seeing senior party members on the roof of the party headquarters including Jorida Tabaku, Grida Duma and Ervin Salianji, who both filmed themselves from within the building and posted the videos on Facebook.

Police arrived at the scene and used tear gas to disperse the protesters. Numerous injuries were reported.

“Protesters repeatedly smashing a sledgehammer against the doors. Others propped up ladders to scale the walls of the building”

Bardhi spoke to reporters the previous day, accusing a minority within the party of seeking to “replace the legitimate DP institutions with acts of violence”.

“The US is deeply concerned with rising tensions at the Democratic Party headquarters building and protesters’ use of force. We call on protest organisers to reject violence and exercise calm. Those inciting violence or undermining the rule of law will be held accountable,” US ambassador to Tirana Yuri Kim wrote on Twitter.

In December, Berisha hosted an unauthorised assembly of Democratic Party members at Tirana stadium, where delegates voted overwhelmingly to oust Basha. The meeting took place after Berisha’s tour of the country to drum up support among Democratic Party members.

However, Basha said he wouldn’t give in to pressure from Berisha to quit. At a meeting of the party’s national council on December 12, headed by Basha, a statement was adopted declaring that all the steps taken at the previous day’s assembly were illegal.

Basha decided to exclude Berisha from the Democrats’ parliamentary group after the latter was named by the US State Department as persona non grata due to his involvement in “significant corruption” in May.
“In his official capacity as prime minister of Albania in particular, Berisha was involved in corrupt acts, such as misappropriation of public funds and interfering with public processes, including using his power for his own benefit and to enrich his political allies and his family members at the expense of the Albanian public’s confidence in their government institutions and public officials,” the May statement from the State Department said.

Berisha dominated the political scene as prime minister and president from 1991 to 2013. He was Albania’s second post-communist president, holding the post from 1992 to 1997, going on to become prime minister from 2005 to 2013, which makes him Albania’s longest-serving democratically elected leader. He twice headed the Democratic Party, which has been in opposition since he resigned in 2013, when the Democrats were ousted from power by the Socialists led by Albania’s current prime minister, Edi Rama.

Basha was mayor of Tirana from 2011 to 2015, having previously served as first minister of public works, transport and telecommunications and later as interior minister under Berisha.

After the loss of the April 2021 election – which Basha called an “electoral massacre” and claimed was rigged – several high ranking members of the Democratic Party called on him to resign. However, he successfully stood for re-election as party leader in the summer leadership election.

Kosovo has informed the EU about its intention to apply for EU membership, the Council of the EU said on December 7.

Kosovo declared independence from Serbia in 2008, but it is still not recognised by Belgrade as a separate state. Five EU members also do not recognise Kosovo. This effectively stymies its progress towards EU accession until a resolution is reached with Serbia, which is already in the midst of accession negotiations.

At the meeting in Brussels, the members of the Stabilisation and Association Council (SA Council) reviewed Kosovo’s progress on its European path following the publication of the European Commission’s 2021 report on Kosovo. The parties welcomed Kosovo’s renewed commitment to its European path.

The meeting was chaired by Kosovo’s Prime Minister Albin Kurti. The EU delegation was led by High Representative Josep Borrell, and included Enlargement Commissioner Oliver Varhelyi.

The parties discussed recent developments relating to the fulfillment of the political criteria, as well as the state of play concerning the economic criteria, financial cooperation and implementation of the Stabilisation and Association Agreement (SAA), the Council of the EU said in the statement.

The SA Council members agreed on the need for Kosovo to continue with reforms and required increased focus by all political actors, strengthening of the administrative capacities and an effective coordination structure within the Kosovan institutions.

The parties reiterated the importance of visa liberalisation for Kosovo citizens.

They noted the Kosovan government’s commitment to enhance the rule of law, fight against corruption and organised crime and respect for fundamental rights, as well as to pursue public administration reform and economic development, and support education and employment.

The meeting underlined the importance of constructive engagement in the EU-facilitated dialogue with Serbia to negotiate and achieve a comprehensive legally binding normalisation agreement.

“This is crucial in order for Kosovo and Serbia to advance on their respective European paths. All past agreements need to be respected and fully implemented,” it was said.

Borrell was cited by Kosovan broadcaster RTK as saying that the meeting between Kosovo’s PM Albin Kurti and Serbian President Aleksandar Vucic is unlikely to take place this year. He added that there can be no new high-level meeting until the previous commitments are not implemented.

Borrell said that the establishment of the Association of Serbian Municipalities is part of the Brussels agreements and this part of the agreement must be implemented by the Kosovan side.

Varhelyi said that the dialogue between Kosovo and Serbia needs to be accelerated in order for the Western Balkans to benefit from the economic investment plan, RTK reported.
Organic food, fresh produce, healthy eating. To many minds, these are part of a quintessentially Western craze, compatible only with gleaming Californian open-plan kitchens and European wholefood stores. Vkusvill begs to differ. It has been offering nutritious food to Russia’s health-conscious consumers for 12 years, and with no small degree of success.

It started when Andrei Krivenko noticed how difficult it was to get fresh milk and dairy products in Moscow. Most shops only offered UHT milk, with a long shelf life and a vanishingly small microbe count. Using a billion rubles of his own savings (equivalent to $30,000 at the time), Krivenko started a stall in Moscow’s unglamorous Strogino market selling fresh dairy products. Now, that same idea – fresh and healthy produce – is the basis of a foodtech company with 1,300 stores in 64 Russian cities offering not only dairy, but Vkusvill-branded produce from across the range of foodstuffs. In an exclusive interview with bne IntelliNews, Yury Alasheev of Vkusvill’s board of directors discussed why Vkusvill resonates with Russians and how the company coped with such rapid growth.

Conscious consumption
Just a week ago, at a meeting of the company’s top leaders, Vkusvill re-affirmed its core commitment: making fresh, natural products convenient and affordable for everyone. “We believe that that’s a total disruption to the market,” said Alasheev.

The figures corroborate this assertion. “We’re the fastest-growing FMCG brand in Russia,” Alasheev pointed out. “And that’s not calculated on a low base – we’re also the largest FMCG brand in Russia. There’s a lot of demand for what we offer.”

That offering can be summarised as conscious consumption. Vkusvill’s model consists of selecting a range of products which are organic, fresh, and free from additives or harmful products. That means that it doesn’t sell sugary carbonated sodas, vodka or double-pasteurised milk. It vets the products on the shelves to ensure that they are conducive to a healthy diet, so that shoppers can be confident that whatever they buy will be good for them.

Already in the top three retailers in Russia’s capital, Vkusvill soon expects to be selling more than European giants, with an estimated top-line growth of over 40% this year. This popularity
has put paid to the myth that healthy eating is the preserve of a Western clique of super-mums. With Russian life expectancy at a record high (73 years), market researcher GfK says that 58% of Russians now take health factors into account when they shop. “We believe that more and more people will opt for fresher and healthier choices and conscious consumption,” Alasheev said. “And that includes fewer food miles and a better internal culture in the company,” he added.

**ESG**

These last points led to the question of ESG. When asked about ESG initiatives, Alasheev seemed slightly puzzled. “We aren’t just doing some initiatives, our whole essence is ESG… First of all, we don’t sell bad products. This is our whole appeal – we propose products which are socially responsible. If you shop with us, you won’t be able to buy cigarettes, you won’t be able to buy vodka, or even popular sweet beverages. We consciously lose sales: if we offered cigarettes in our convenience stores, we would be getting more, but we refuse to do that,” he explained.

“The other thing we do is to work predominantly with local small and medium enterprises,” Alasheev said. “So among our suppliers you won’t see globally available huge multinational companies. It’s predominantly smaller, local businesses. By doing that, we support the territories we’re operating in. Also, it gives us the ability to have low food miles. Since we sell fresh products, we’re offering things which are mostly produced nearby.”

“But on top of that, we are the largest battery collector in the country, and we have recyclable packaging and all that stuff,” Alasheev added almost cursorily. “I see these as more standard programmes – we run them, and we are even leading in the country in some of these areas, but to me we are much more than that – starting from our assortment, our supply, and how we work with people inside the company.”

**E-commerce**

But even at this stage in its development, with a clearly articulated mission and 20,000 staff, Vkusvill is still confronted with new challenges as it grows. “If you ask anyone, I think, they’ll tell you that the largest thing in the last year has been the move online,” said Alasheev categorically. “As consumers turn to online formats, it’s now a growing market, with triple-digit numbers. The biggest challenge at the moment is how to address that. We have a new set of competitors coming into the foodtech and retail market, and these new competitors are used to working in markets where they can afford to work on narrow margins - coming from the technology side, for example,” Alasheev said.

Indeed, the appearance of e-grocery companies backed by tech company Yandex and banking giant Sberbank demonstrates what a diverse range of players are throwing their hats into the ring, hoping to secure a slice of the very lucrative grocery delivery market.

Alasheev clearly has no illusions about how competitive this process will be, but he seems upbeat about it, confident that Vkusvill has the edge. As recently as 2020, Vkusvill had close to zero e-commerce presence. Now, it is the leading player in Moscow for online groceries. Just like its growth from a single dairy stall to a chain of stores, Alasheev puts this explosive increase in trade down to innovation, experimentation, and simply good ideas. “We were one of the first in Russia to deliver for free with no minimal limit,” he points out. In addition to its 100 dark stores, Vkusvill also dispatches deliveries from its normal stores, meaning it can

“We’re the fastest-growing FMCG brand in Russia. And that’s not calculated on a low base – we’re also the largest FMCG brand in Russia. There’s a lot of demand for what we offer”

**Yury Alasheev**, Member of the Board of Directors, VkusVill
reach a greater range of houses in a much faster time.

One intriguing dimension of the shift to e-groceries is that online customers simply buy more, so the stakes are higher for retailers. "The average purchase is almost three times larger," Alasheev confirmed. "For some reason, when people shop offline, it’s ok to drop in at several shops. But online, where you would have thought that it’s easier to just close the application, open a new one, and make another order, that’s not the case. Online, people are less inclined to make several orders. Because of that, they tend to buy more when they go online."

Beyond Taylor
Vkusvill’s success – even through two waves of incredibly rapid expansion – is built on a very unusual philosophy. The company espouses a management system called ‘Beyond Taylor’, which involves dispensing with the traditional layers of corporate hierarchy in favour of a much leaner system which puts people first: "Businesses are mostly oriented on eliminating the human factor, considering it as a kind of problem for the business," Alasheev lamented. "And the instruments for that are things like KPIs, job descriptions, control of performance. We don’t have any of that stuff."

The idea behind favouring independent teams over departments is that it gives each individual more freedom and more scope for creativity and experimentation. "If you take a store, that’s a self-managed team - they don’t really have a boss, they operate on their own. And that’s what people need, basically... When you have a goal without anyone telling you what to do, and you achieve that goal, it’s very good motivation, and a source of enthusiasm and joy. That’s why we see that people can spend thousands of hours on computer games without being paid for it. We’re trying to re-create that in the work environment. If, rather than being told what to do, you play the game yourself and then simply discuss what you achieved, both the game and the discussion of what you achieved become fun."

A workplace where everyone is an associate, without dress codes, fines, bosses, or budgets sounds rather utopian. But does Vkusvill have any evidence that this model is more effective than the traditional management structure? Alasheev shrugged. "This model allowed us to build the largest food brand in Russia. This model allowed us to build a company from scratch, profitable from day one. It was paid completely with our own money. We have no bank debt, and we always raise money in the company. So that’s evidence in itself."

Another virtue of the Beyond Taylor management system is the agility it brings. As a foodtech brand working with huge data sets, quick responses to subtle market changes are of the essence for Vkusvill. When the company had to scale up its online offering in response to the pandemic, for example, it managed to bring its share of online sales from zero to thirty percent in just a year. Alasheev attributes this feat of logistics to a nimble, people-oriented model. "It’s not bureaucracy, but humanocracy. We didn’t need to re-write the job descriptions, to re-arrange our departments or re-negotiate a new set of KPIs. We could jump straight into the task."

"This model allowed us to build the largest food brand in Russia. This model allowed us to build a company from scratch, profitable from day one. We have no bank debt, and we always raise money in the company. So that’s evidence in itself.”

Reports have been circulating that Vkusvill is mulling an IPO, but Alasheev insists that the company is considering a much broader range of mechanisms to fuel future growth. "For our 12.5 years of existence, we’ve managed to finance our growth on our own, without tapping any financial markets. But since right now competition in e-grocery is more fierce, we are considering some of the financial markets – equity, financial, strategic investment. We’re open to all options."

www.bne.eu
Belarus’ opposition leader Tikhanovskaya calls on the people to hold firm in an emotional New Year’s address

Belarusian opposition leader Svetlana Tikhanovskaya told viewers that she was “angry” but sees “light in the darkness: you,” in a slick New Year’s address released on YouTube (with English subtitles) to see out a year of frustration and repression for her country.

“We thought it shouldn’t be so long, so difficult, there shouldn’t be so many losses. We wanted a new country and a new future,” Tikhanovskaya said in a high quality and professionally produced clip. “And I am also angry that in response to this, Belarusians received revenge, violence and crisis.”

She went on to pay tribute to those that had lost their lives as a result of the brutal repression unleashed by Belarus’ President Alexander Lukashenko, who claimed a landslide victory in last August 9 presidential elections that are widely seen as massively falsified.

“I am also scared: what if the regime takes another life? What if we don’t have enough strength? What if our kids have to start all over again? What if all this path, in which so much work, love and faith is invested, does not lead to victory?” Tikhanovskaya asked, addressing the frustrations and fears of many after a year and half of protest that has brought the opposition no nearer to ousting Lukashenko.

However, she appealed to the people to remain firm in their resolve to change the political system and lauded the people as the strength of the country.

“All this time, even on the darkest days, I see the light – because I look at you,” the former housewife turned revolutionary said as the lights on the set rose to reveal several other leading figures in the opposition movement, including Pavel Latushko, a former Culture Minister in Lukashenko’s government turned rebel and now in exile. “To those who say "this is our land and we will not go anywhere".”

She praised the Belarusian people for their creativity and ability to endure and flourish even in harsh conditions.

“Now our victory is no longer a matter of chance or luck. It is a matter of our determination,” Tikhanovskaya said. “Willingness to take the fate of the homeland into their own hands and every day to go to the new Belarus, which we all dream of. ”

Tikhanovskaya’s speech was in stark contrast to Lukashenko’s own New Year’s message that played on the economic chaos of the 90s and the stability he brought to the country by creating a neo-Soviet system, for which many Belarusians remain grateful.

“This is how our sovereign state has been built and prospered for 30 years, painstakingly, day after day. And agree, looking back to the early 90s, we have something to be proud of. We have built a modern, stable and successful country,” Lukashenko said.”

Navalny wins Sakharov prize, but European Parliament spells his name wrong

The European Parliament awarded jailed opposition figure Alexey Navalny with the prestigious Sakharov Prize for Freedom on December 15, but spelled both his name and the word “corruption” incorrectly on the certificate.

In an embarrassing gaffe, the certificate collected by Navalny’s daughter at a ceremony in Strasbourg had the typos on the official certificate, causing much scoffing on social media.

“It speaks volumes about the West’s problematic attitudes towards Russians when European Parliament can’t even spell Navalny’s name, as well as the word “corruption”, correctly in Russian, a major European language, native to millions of EU citizens. On Navalny’s own award!” bne IntelliNews contributor and well known journalist Leonid Ragozin said on twitter.

Navalny was poisoned last year and medevaced to Germany to recover. He was arrested on his return to Russia in January and sentenced to 2.8 years in jail for breaking the terms of his parole from an earlier conviction, which he claims was politically motivated.

Navalny’s daughter collected the award named after the Russian physicist and Nobel Peace Prize winner on her father’s behalf.

The certificate, written in Russian, had two spelling mistakes in it: Navalny’s name was written as “Aleskey” and the word corruption lost one “r.” The certificate was signed by the European Parliament’s president, David Sassoli.
A rocket launch facility set to begin construction next year in southern Kazakhstan is to be named after former president Nursultan Nazarbayev, a senior official has said.

The Nazarbayev Start, which is being built jointly with Russia at the Baikonur cosmodrome, will accommodate new-generation craft designed to have a reduced environmental impact compared to those currently in use.

Digital Development, Innovation and Aerospace Industry Minister Bagdat Musin said on December 14 that a definitive decision on whether the facility will retain Nazarbayev’s name will be made after initial construction work is complete.

The idea to bestow the former Kazakh leader’s name upon the launchpad appears to have initiated with Russian President Vladimir Putin in 2019.

The intended purpose of the new platform is to launch Soyuz-5 vehicles, which will run on relatively clean naphthyl fuel, instead of the toxic heptyl required by the heavy-lift Proton rocket currently used to carry heavy cargo into space.

Spills of heptyl rocket fuel over Kazakhstan’s land in the past have bred strong resentment over operations at Baikonur, which is under lease to Russia until 2050. Moreover, Kazakhstan has seemingly struggled to secure adequate compensation for these incidents.

Construction of the new complex has been serially delayed since an initial agreement on the project between Kazakhstan and Russian was reached in 2004. Cost estimates have ballooned around sevenfold to $2bn as the joint developers failed to agree on what launch vehicle was to be used at the facility.

Nur-Sultan and Moscow only managed

“The idea to bestow the former Kazakh leader’s name upon the Launchpad appears to have initiated with Russian President Vladimir Putin in 2019”
to resolve all their differences on October 2020, at which point they inked a definitive agreement.

Kazakhstan has undertaken to spend 91bn tenge (US$208mn) on an overhaul of the launch complex on which Nazarbayev Start is to be built, while Russia is developing and constructing the Soyuz-5 at an estimated cost of US$916mn. Russia has committed to launching craft from the Nazarbayev Start at least twice yearly over the period of a decade, ensuring predictable revenue, Musin told lawmakers in November.

Construction of what is, for now, being known as the Nazarbayev Start is slated to begin in March and be completed a few months before flight tests start in December 2023.

Russia is especially eager not to see those deadlines slip.

“It is extremely important for us to see the light at the end of the tunnel,” Roscosmos space agency chief Dmitry Rogozin said at an intergovernmental commission meeting in Nur-Sultan on December 13.

Almaz Kumenov is an Almaty-based journalist.

This article originally appeared on Eurasianet.

Tensions as US imposes more sanctions on Iran ahead of next Vienna nuclear talks

Ben Aris in Navoi

There were fresh tensions between Iran and the US ahead of an expected December 9 return to the Vienna nuclear deal talks after the Biden administration imposed fresh sanctions on Iranian entities and officials. Tehran warned Washington it should not calculate that the measures would “create leverage” in the negotiations, called as attempts continue to find an agreement that would restore Iranian and American compliance with the deal, known as the JCPOA.

The US Treasury Department blacklisted the Special Units of Iran’s Law Enforcement Forces and Counter-Terror Special Forces and several officials linked to the agencies, accusing them of human rights abuses.

Rebuking the US for announcing the sanctions on the eve of the next stage of the talks, Iranian Foreign Ministry spokesman Saeed Khatibzadeh, referencing the former Trump administration’s “maximum pressure” strategy directed at Iran, said on Twitter: “Washington fails to understand that ‘maximum failure’ & a diplomatic breakthrough are mutually exclusive. Doubling down on sanctions won’t create leverage – and is anything but seriousness & goodwill.”

The JCPOA was signed by Iran, the US and five other major nations in late 2015. It tied Iran to compliance with terms that would ensure its nuclear development programme was kept entirely civilian. In return for the compliance, heavy economic sanctions were lifted. But in May 2018, then US president Donald Trump unilaterally abandoned the multilateral deal, arguing it should be tougher on Iran, and brought in sanctions aimed at crippling the Iranian economy. In response, Iran has gradually moved to a point where its nuclear activities breach the JCPOA in numerous and substantial ways.

Fear of next US president

A problem with current US President Joe Biden’s wish to resurrect the deal with full Iranian and American participation is that even if sanctions are lifted, it is unlikely that many foreign investors will return to Iran as they will fear that the next US president, should he or she be a Republican, will reimpose the sanctions. Given the situation, there are arguments that it might suit Iran, the US, the remaining JCPOA signatories and Israel – which, despite persistent denials
from Tehran, claims the Iranians are intent on developing nuclear weapons – to conclude the Vienna talks with the “coma option”.

The option has been described by Trita Parsi, executive vice president of the Quincy Institute. Under the scenario, explained Parsi, in which the negotiations to resurrect the nuclear deal have become almost deadlocked, the JCPOA “would all but die, but the parties would pretend that it is still alive to avoid the crisis that its official death would spur. Let’s call it the coma option. Think of how Western powers have pretended that the Israeli-Palestinian peace process has been alive for the last decades”.

The US last week accused Iran of walking back previous diplomatic progress made in the Vienna talks earlier this year.

However, neither the US nor Israel are making the case that an Iranian nuclear bomb could be imminent. Israel has lately stated that Iran is likely around five years from having a nuclear weapon if its current rate of development progress continues, while William Burns, director of the CIA, on December 6 told The Wall Street Journal’s CEO Council Summit: “We don’t see any evidence as an agency right now that Iran’s supreme leader has made a decision to move to weaponize [nuclear know-how]”.

Burns described Iran’s challenge as “a three-legged race” to obtain fissile material, to “weaponize” by placing such material into a device designed to cause a nuclear explosion and to mate it to a delivery system such as a ballistic missile.

On weaponization, Burns said “the Iranians still have a lot of work to do there as far as we judge it”.

In first ICJ rulings, Armenia largely comes out on top of Azerbaijan

Neil Hauer in Yerevan

The first rulings in a pair of landmark cases at the International Court of Justice – with Armenia suing Azerbaijan for inciting racial hatred and abusing prisoners of war and Azerbaijan’s countersuit on anti-Azeri racism in Armenia – have largely gone in favour of Yerevan.

On December 7, in the first case (Armenia vs Azerbaijan), judges at the ICJ examining Armenian allegations that Azerbaijan breached a convention against racial discrimination ordered Azerbaijan to prevent incitement of racial hatred against Armenians and protect Armenian prisoners of war.

The statement included a demand that Azerbaijan must “take all necessary measures to prevent the incitement and promotion of racial hatred and discrimination including by its officials in public institutions targeted at persons of Armenian national or ethnic origin”.

Presiding judge Joan Donoghue said Azerbaijan must protect from violence and harm “all persons captured in relation to the 2020 conflict who remain in detention” and must “prevent and punish acts of vandalism and desecration affecting Armenian cultural heritage”.

The same day, in the second case (Azerbaijan vs Armenia), the first rulings were also issued. In the court statement, the ICJ ordered Armenia to “take all necessary measures to prevent the incitement and promotion of racial hatred, including by organizations and private persons in its territory, targeted at persons of Azerbaijani national or ethnic origin”. As for another Azerbaijani request, regarding a call to prevent Armenia destroying evidence of ethnically motivated crimes against Azerbaijanis, the court found these measures “are not warranted”.

Analyzing the outcomes of the two initial rulings, human rights lawyer Gabriel Armas-Cardona that regarding the protection of Armenian cultural sites, the ICJ “gave Armenia everything it asked for”. For the second suit, meanwhile, Armas-Cardona noted with surprise that Azerbaijan had received “only 1 of its 6 requests” in its ICJ suit, fewer than expected.

Armenia filed its ICJ suit on September 16. Azerbaijan filed its countersuit on September 23.
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There is very little chance that Russia will invade Ukraine, but the deals that Russian President Vladimir Putin is asking for will in effect return Europe to Cold War-like relations with Russia.

MOSCOW BLOG

Russia won’t invade Ukraine.
This crisis is more serious than that

Ben Aris in Berlin

ewspapers have been gleefully reporting about a “possible” invasion of Ukraine by Russia since the end of October. But analysts – both Russian and international – are almost unanimous in the belief that the chances of an actual invasion are almost zero.

As bne IntelliNews has reported in detail, the reasons are obvious: it would be too costly in Russian lives, something that Russian President Vladimir Putin’s slowly falling approval and trust ratings make extremely unappealing to the Kremlin; while Russians overwhelmingly support the annexation of Crimea, they are a lot more uncomfortable with the war in Donbas; eastern Ukraine could be taken easily, but western Ukraine could not; and finally the international diplomatic backlash would be catastrophic for Russia’s economy.

And why bother? What would Russia gain? The only thing of value Ukraine has is agriculture, which would collapse in the event of an all-out war followed by an inevitable vicious and impassioned insurrection. On top of that, the Kremlin would take on the cost of fixing Ukraine at a time when it is struggling to fix Russia Inc. It’s not going to happen.

So what is actually going on here? As usual, all you have to do is listen to what Putin says. Putin has a history of telegraphing his moves well in advance. That was the big difference between Putin and his predecessor Boris Yeltsin, who never said what he meant.

In Putin’s big set-piece speeches he lays out his plans in black and white and almost always follows through on them. But as it is Putin and as he has been so demonised in the last two decades a lot of what he says is ignored, or twisted to suit the various narratives used to describe Russia.

Putin said in his very first speech as president that demographics was the main danger to Russia and as we
reported in “Putin’s babies”, he did something about that a decade later. Putin warned in his 2007 Munich Security Conference speech that Russia would push back if its security concerns were ignored and he started modernising the army in 2012, annexed the Crimea in 2014 and is now moving up troops that could invade Ukraine in 2021. You can draw a straight line through all these points.

What did he say?
Putin has just done it again. During the Munich speech he brought up the broken verbal promises made to Mikhail Gorbachev of no Nato eastern expansion. And he has mentioned them again in the last month several times.

The year after Munich in 2008 the Russian Foreign Ministry drew up detailed plans for a new pan-European security deal that included a fair specific framework proposal released by the Russian Foreign Ministry in 2009. Putin has now brought that up again, demanding “legal guarantees” from Nato that it will not expand further (i.e. allow Ukraine or Georgia to join). The Russian Foreign Ministry followed up a few days after the two-hour December 7 virtual summit with Biden with a concrete five point list of demands and on December 15 the MFA sent even more extensive details on what a security deal could look like. Clearly the MFA has been working on this for some time and has a very clear idea of what it wants.

There is a general assumption that the current war talk will die away in the New Year. Daniel Salter, head of Equity Strategy and head of Research at Renaissance Capital, said during a conference call on December 16 that Russia is one of the more prospective investment stories in 2022, as the house view is that Russia won’t invade Ukraine and that things will “calm down”.

It’s clear to everyone that Putin is dead set against Ukraine joining Nato, but the assumption is that he is satisfied with the frozen conflict he has caused in the Donbas because that guarantees Ukraine can never join Nato. So after the current posturing is over the status quo will resume.

And that is the bit that has changed.

New Deal
If you listen to what Putin has been saying he is no longer happy with the status quo of maintaining a costly and embarrassing insurrection in the Donbas. He wants a resolution of the Nato question. He wants the promises made to Gorbachev fulfilled and guaranteed. He wants the status of Ukraine in Europe defined. And he wants the West to stop interfering in Russia’s affairs.

Again, all this was laid out in black and white by Russian Foreign Minister Sergei Lavrov in his new rules of the game speech in February and again a month later when he said Russia would break off diplomatic relations with Europe if the West continued its policy of sanctioning Russia. To underscore the point the Kremlin did break off diplomatic relations with Nato in October.

Things won’t calm down in the New Year if the West does not take these demands seriously. Russia will not withdraw its troops from the Ukrainian border regions until meaningful progress has been made on starting these talks. Lavrov made it clear in his speech that Russia has set the bar at zero tolerance and is not prepared to compromise or make concessions with the West unless the West moves first.

In the meantime, Russia will continue its military preparations. It will continue to build up its economic and military ties with Beijing, which has exactly the same agenda. Pointedly eight days after Putin’s summit with Biden, Putin held the same online summit with China’s President Xi Jinping where they pledged their mutual friendship on what was clearly intended as a message to Washington: you cannot divide the Russian and Chinese “problems” unless we are prepared to co-operate.

Thrashing out a new security deal will be extremely difficult. Both sides of the House in the US are strongly critical of Russia and after the Afghanistan debacle Biden is keen to show that the US will stand by its allies, said Renaissance Capital’s chief economist Charles Robinson at the same briefing. That means supporting Ukraine in its conflict with Russia and maintaining Nato’s compelling deterrent.

However, it appears that Biden has already agreed to a more comprehensive deal with Putin than was revealed in the post December 7 summit comments.

Biden backed talks between four “leading members” of Nato and the Kremlin to discuss Putin’s demands within days. Putin restored all the machinery of diplomatic relations with the US that have been frozen since the summer following

“If you listen to what Putin has been saying he is no longer happy with the status quo of maintaining a costly and embarrassing insurrection in the Donbas. He wants a resolution of the Nato question”
US joining the Normandy Four group that is trying to broker a peace deal in Donbas.

Likewise, in Europe the new German Foreign Minister Annalena Baerbock said last week that the certification for the Nord Stream 2 gas pipeline would be suspended “if Russia invades Ukraine”, but in the meantime Germany has suspended arms sales to Ukraine via its state procurement agency.

Biden continues to make very tough statements about the severity of the response “should Russia invade Ukraine,” but increasingly this is looking like a smokescreen that allows Biden to appear strong, but actually buys him the room to engage with Russia on the more subtle job of working out a workable deal with Putin.

Most of the war talks that started at the end of October have been driven by US intelligence briefing US newspapers. “One scenario that a Democrat party member told me,” says Robinson, “was that you can talk tough about Ukraine’s invasion, but when it doesn’t happen then somehow the US and Biden can take some credit for that not happening.”

In the New Year a much more difficult process starts of the Kremlin negotiating with a reluctant Washington on a new security deal. At this point it is not clear if Washington is even willing to contemplate any sort of deal at all. However, if that happens then Putin is very likely to turn up the temperature again and cause a fresh flaring in tensions – possibly with the increasingly participation of China.

**New Cold War**

What Putin is proposing in effect is a return to the Cold War relations between East and West. And many of those security arrangements are reappearing.

In this sense the current showdown is better understood as a modern version of the Cuban Missile Crisis where Putin, like John F Kennedy, finds the possibility of western missiles on Ukrainian soil, a few minutes flight time to the largest part of Russia’s urban population, anathema. Like in 1962 no one actually wants to go to war and are willing to do a deal, but like then the threats of war are serious and remain a real possibility.

Russian Deputy Foreign Minister Sergei Ryabkov has explicitly compared the current crisis to the Cuban Missile Crisis and went on to say on December 13 Russia may be forced to deploy intermediate-range nuclear missiles in Europe in response to what it sees as NATO’s plans to do the same.

Ryabkov said if the West did not engage in the talks that Putin is proposing the Russia would escalate by moving missiles west. Specifically he said if the West declined to join it in a moratorium on intermediate-range nuclear forces (INF) in Europe, that is included in the Russian Foreign Ministry’s list, “It will be a confrontation, this will be the next round,” he said, referring to the potential deployment of the missiles by Russia.

Poignantly Ryabkov said Russia has a "complete lack of trust" in Nato, which was the basis of the Cold War thinking. "They don't permit themselves to do anything that could somehow increase our security - they believe they can act as they need, to their advantage, and we simply have to swallow all this and deal with it. This is not going to continue,” Ryabkov added, echoing Lavrov’s "new rules of the game" speech.

Another trope of Putin’s is to complain about the US unilateral withdrawal from the ABM missile treaty in 2002, a key piece of the Cold War security infrastructure. The decision marked the end of the bonhomie between Putin and Bush and arguably started Russia off on the road that would lead to the current clash.

Following that, the US withdrew from several other Cold War treaties, with the most recent being the US nixing the Intermediate-Range Nuclear Forces Treaty (INF) and Open Skies treaty under Trump.

One of the positive signs in the prospects for a deal between Biden and Putin is that the US president is in favour of these old deals and was vocally opposed to the US exit from the ABM treaty while he was a senator. Moreover, in the first week on the job Biden rushed through renewing the START III missile deal and broached the topic of new arms deals during his meeting with Putin in Geneva.

For its part the Kremlin is also keen to see these deals back in place and one of the items on the Russian Foreign Ministry list is to restart the INF treaty, which was also mentioned by the Russian side when the START III deal was done in January.

However, this set-up is to concede that all hope of friendly relations between Russia and the West are over. Security will be based on arms controls deals, backed by the threat of force. Russia is now actively avoiding engaging with multilateral organisations other than the UN, where it has a veto, and the G20, where it is actively building a network of allies and illiberal and barely democratic countries are in the majority.

But this set-up will bring peace and quiet. It could end the war in Donbas relatively quickly. And it could mean that Putin steps down as president in 2024, as he is clearly tired of the job, but Ukraine's status is his big legacy issue and he won't leave as long as that is unresolved.
The end of 2021 was marked by hair-raising confrontation between the two greatest nuclear powers, the US and Russia, over Ukraine - a country defending itself against Russian aggression since 2014. It suddenly felt like the ghost of the Cuban missile crisis has come to life, threatening us with nuclear Armageddon.

It was the culmination of a year-long standoff, which began with the Biden administration and its Ukrainian allies attempting a more assertive policy towards Russia.

In a major change of tack, which coincided with Biden’s arrival in the White House a year ago, President Volodymyr Zelenskiy made several moves that were meant as a slap to Russian President Vladimir Putin’s face.

He sanctioned Russia’s ally in Ukraine, Viktor Medvedchuk, and outlawed TV channels associated with him. He brought the issue of Russian-occupied Crimea back into the spotlight by announcing the Crimean platform. Most irritatingly for the Kremlin, he launched a campaign, co-ordinated with influential DC lobbyists, for Ukraine’s membership of Nato.

That, quite expectedly, triggered Moscow’s heavy-handed response. By April, nearly 100,000 Russian troops were deployed not far from the Ukrainian border in a menacing show meant to signal Putin’s readiness to go to war, should one of his “red lines” be crossed by the perceived adversary.

The interim result of this year-long confrontation, now interrupted by US President Joe Biden and Putin agreeing to launch negotiations, can be illustrated by two publications on the website of the Atlantic Council – a Nato-linked think-tank, which advocates hawkish policies towards Russia.

The first one, released a couple of weeks before Russia started pulling troops to the Ukrainian border in March 2021, was a proposed Ukraine strategy for the Biden administration. The document called for granting Ukraine a membership action plan for Nato should Russia prove “intransigent” in peace talks. It called for arming Ukraine and stepping up Nato’s naval activities near Russian shores in the Black Sea. Finally, it unequivocally stated the goal of derailing the Nord Stream 2 pipeline project, which would allow Russia to supply gas to Western Europe bypassing Ukraine.

The second Atlantic Council document, signed by an even more stellar cohort of American diplomats and top brass military commanders, was published in the last days of 2021. The goals it set were markedly less ambitious. It contained no more talk about Nato membership plans for Ukraine and only mentioned Nord Stream 2 in the context of putting pressure on Berlin into suspending the project, should Russia invade. But it still called for providing weapons to Ukraine and for a more assertive military posture in the Black Sea.

As the dust settles, Putin has good reasons to believe that his blackmailing of the West with the prospect of full-out war in Ukraine has worked. Nato membership is clearly off the table, with Russia having embarked on a counter-offensive and demanding that Nato guarantees its non-expansion into post-Soviet space.

Nord Stream 2 is completed and awaits certification by the German regulator. Despite token gestures towards the US allies, Berlin appears to be largely unfazed by the Russian invasion panic which was fanned by the Biden administration at the end of 2021 in the last-ditch attempt to shut down the project, with the newly formed German government as the target audience.

The only real big loss for Putin is Medvedchuk’s exclusion from political life in Ukraine at the start of the new election cycle. That diminishes Russia’s chances of altering Ukraine’s course by political means. But there is no doubt that Putin will keep trying to salvage his protégé.

But the most significant result of the standoff is clarity. Putin demonstrated where his red lines are, beyond which the prospect of war becomes all too real. He means it. The prospect of Nato in Ukraine raises the same kind of panic as Soviet missiles in Cuba did in the US. Putin knows he will have Russian society rallying behind him if that prospect becomes

Leonid Ragozin in Riga

Following the fall of the Soviet Union the West welcomed most of the countries of the Former Soviet Union into the trans-Atlantic family except one – Russia.
real and he will need to act. He benefits from confrontation through adversarial legitimisation. It prolongs his political life.

But in setting out his own red lines, Putin also exposed America’s own limitations with regard to Ukraine. Towards the end of December, the US administration was making it abundantly clear that it would not sacrifice American soldiers for the Ukrainian cause. At the end of the day, Russia proved that it cares more about Ukraine’s future than the US does and it is prepared to make significantly greater sacrifices to keep its most important neighbour militarily and politically neutral.

There is symbolism in the fact that it happened right at the time when ex-Soviet people were marking the 30th anniversary of the collapse of the USSR. It’s not just Biden’s attempt to change the Ukrainian equation, which hit the wall in December 2021, but the entire set of policies implemented by successive American administrations in the ex-Soviet space over the last 30 years.

These policies boiled down to alienating Russia from its closest neighbours by the means of welcoming and actively nudging every East European country towards Euroatlantic integration, while explicitly denying that prospect to just one country – Russia. It was never properly articulated in public or put to open debate. Rather, it developed on an ad hoc basis, as a sum total of disappointments with Russia’s deficient democracy in the 1990s, a deeply ingrained xenophobia towards Russians, greatly fuelled by America’s newly acquired allies in Eastern Europe, and the loss of the enemy by Cold War hawks and the military-industrial complex they are being paid by.

The divergence of perceptions began right at the time when Russians defeated the communist regime in the August 1991 revolution, precipitating the collapse of the USSR four months later. The Russians saw the end of the USSR as a common victory, achieved together with the West. But in no time then-president George Bush Sr. was already announcing the US victory in the Cold War.

Despite that, there was still an immense enthusiasm for embracing the West in the Russian Federation – a new country that emerged as the largest fragment of what used the Russian Empire and Soviet Union. A poll conducted by Levada Centre in November 1991 showed 80% of Russians having a positive attitude to the US; compare it with 12% in January 2012.

The Russians were emerging from a totalitarian sect, into which the vast majority of them were born and thus deprived of crucial knowledge as to how the outer world worked. Dazed and confused, they immediately plunged into the wild world of capitalism accompanied with social Darwinism of the Novi Russky new rich, extreme poverty, rampant crime and regional wars.

They surely are to blame for many bad choices made in the following decades. Yet it was the American-led West which should have been the adult in the room. But despite its messianic ambition of spreading democracy around the world, the West shamefully failed in this role, triggering a domino chain of events that led to the current standoff.

Throughout the 1990s, the Russians were patiently waiting for their turn to be invited to the Euro-Atlantic club, sensing – with their characteristic self-deprecation – that they could be unworthy and it was all their own fault. But towards the end of the decade, it started dawning on the political establishment in Moscow that despite all the smiles and token gestures like Russia-NATO council of G8 membership, the US was playing the good old geopolitical chess in which Russia was not an ally, but a rival.

The West’s indifference bordering on sympathy towards Chechen terrorism and its divide-and-rule policy in the Balkans all contributed to the changing attitudes. But Nato expansion was always the main grievance. From Russia’s perspective it all amounted to a creeping Versailles.

In 1999, Moscow Mayor Yuri Luzhkov wrote in a Kommersant op-ed: “Through its expansion and military action [he was referring to the bombing of Belgrade], Nato essentially provokes Russia into self-isolation and nurtures sieged fortress sentiments. Such a fortress would be a gift to those circles in Nato which are still seeking a justification for their mighty arsenal and military programmes”.

Back at the time, Luzhkov formed a tandem with prime minister Yevgeny Primakov fighting for power against Yeltsin’s young nominee for president – Vladimir Putin. They were seen by Russian liberals and the West as conservative dinosaurs standing in the way of progress and further rapprochement with the West. The latter was firmly on Putin’s side in this rivalry.

Luzhkov’s article turned out to be prophetic. As the West set itself on a collision course with Russia by expanding Nato and starting – right at the same time – to counter Russian energy projects in Europe, Putin’s Russia began moving, very slowly and gradually, towards self-isolation and authoritarian rule. Its behaviour was now dictated by the logic of a larger and far more powerful nuclear monster than Russia itself encroaching on its immediate neighbourhood.

The vector of Russia’s development and Putin’s personal evolution as a leader was predetermined by the bad strategic choices made in Western capitals. As it deals with an extremely intransigent and unpredictable Putin in 2022, the West is facing its own Frankenstein.

The war in Ukraine is the collision moment in this confrontation. A more direct involvement of the West will open up a truly apocalyptic prospect for the whole world.

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The West’s tricky relationship with Kazakhstan gets more complicated

Clare Nuttall in Glasgow

Western government officials have long had to reconcile their desire for Kazakhstan’s vast natural resources with the country’s poor record on democracy and human rights.

The eruption of violent protests and their brutal suppression make this relationship more difficult, and the arrival of troops from Russia and other member states of the Russian-dominated Collective Security Treaty Organisation (CSTO) at the request of President Kassym-Jomart Tokayev is no doubt an unwelcome development.

Ever since independence more than 30 years ago Kazakhstan’s long-serving former president Nursultan Nazarbayev pursued a multi-vector foreign policy that combined very close relations with Russia – Kazakhstan was one of the founding members of the Customs Union that later grew into the Eurasian Economic Union – with friendly relations with a broad range of countries from the West, the Middle East and Asia.

However, the latest developments have re-positioned Kazakhstan firmly in Russia’s backyard, as Tokayev relies on soldiers from Russia and other counties within Moscow’s sphere of influence to re-establish control over the country.

The post-independence oil rush

When the Soviet Union broke up, western oil companies were quick to move in to develop the oil and gas resources of the Caspian Basin in both Kazakhstan and Azerbaijan that had been previously behind the Iron Curtain. As early as 1992, AGIP (now Eni) and British Gas were awarded negotiating rights for Kazakhstan’s Karachaganak field, later signing a production-sharing agreement (PSA) with the Kazakh government alongside Texaco (now Chevron) and Russia’s Lukoil. Another international consortium later started developing the Kashagan mega field.

Kazakhstan’s geo-strategic importance, and that of its Central Asian neighbours, suddenly increased with the start of the War on Terror after the attacks on the Twin Towers in New York on September 11, 2001. The Muslim yet largely secular states were important allies when it came to the logistics of the war in Afghanistan and as a stable buffer zone north of the war-torn country. Western governments were therefore willing to ignore the repression of these states’ own populations – not least when it came to keeping a lid on any homegrown Islamic fundamentalism on their own territories.

This combination of economics and geopolitics encouraged western politicians to downplay events such as the December 2011 Zhanaozen massacre in Kazakhstan, the worst violence by the security forces against the population until this week’s events.

Just over three months after the shootings in the western oil town, then US president Barack Obama exchanged warm words with Nazarbayev at the March 2012 Nuclear Security Summit in Seoul. Not mentioning Zhanaozen, Obama’s official statement noted the US’ commercial relations with Kazakhstan and added “interested in discussing with the President efforts to further expand democracy and human rights within Kazakhstan, which will help to lead to further growth and prosperity in the future”.

Meanwhile, former British prime minister Tony Blair gave Nazarbayev advice on how to avoid his image being tarnished by the killings in Zhanaozen. His consultancy, Tony Blair Associates, much criticised for advising countries with poor human rights records, signed a multi-million-pound deal to advise Kazakhstan’s leadership on good governance.

Other western government officials wooing Kazakhstan have also struggled to bring together the not very compatible sentiments of ‘let us drill your oil’ and ‘don’t kill protesters’ with an added dash of ‘keep up the good work against fundamentalism’. Politicians on visits to the Central Asian nation have long tended to make some bland statements on human rights and democracy largely for the benefit of the audience at home before getting down to the actual business of natural resources deals and infrastructure contracts.

The traffic has gone two ways; not only have western investors flocked to Kazakhstan; the new class of super-rich Kazakhs favour London and other western cities to buy properties and secure their money. In a December 2020 feature, RFE/
RL identified at least $785mn in European and US real estate purchases made by Nazarbayev’s family members and their in-laws in six countries over a 20-year period.

Their fabulous riches provided an easy entree into international social circles, including with members of the British royal family.

Queen Elizabeth’s disgraced second son Prince Andrew is known to have friendly relations with both the former Kazakh president and his son-in-law Timur Kulibayev. Back in 2007, British media revealed that Kulibayev had purchased Prince Andrew’s former home Sunninghill for GBP15mn ($20.4mn), a steep GBP3mn higher than the asking price.

Several years later, Prince Harry and his then girlfriend Cressida Bonas were photographed at the ski resort of Shymbulak near Almaty, reportedly at the invitation of Kazakh oligarch Serzhan Zhumashov, a friend of Nazarbayev’s.

Kazakhstan erupts

The Nazarbayev family are understood to have fled Kazakhstan by private jet to an unknown destination after violent protests erupted this week, prompting a harsh crackdown by security forces. Russia and its fellow CSTO members zoomed in almost immediately to back up Tokayev’s regime. Russian media reports – the only ones coming out of Kazakhstan aside from the Kazakh state media during the internet blackout – have played up the violence and instability in the country.

US Secretary of State Antony Blinken commented on the arrival of CSTO troops on January 7, saying it was “not clear why they feel the need for any outside assistance”.

“One lesson of recent history is that once Russians are in your house, it’s sometimes very difficult to get them to leave,” Blinken added at a State Department press briefing.

Until then, the main western powers had issued cautiously worded statements appealing to both sides for restraint and to avoid violence. Just like in other post-Soviet countries that Russia regards as firmly in its sphere of influence, there’s very little they can do in practical terms.

As the situation deteriorated on January 5, US State Department spokesperson Ned Price commented: “We condemn the acts of violence and destruction of property and call for restraint by both the authorities and protesters. We ask for all Kazakhstani to respect and defend constitutional institutions, human rights and media freedom, including through the restoration of internet service. We urge all parties to find a peaceful resolution of the state of emergency.”

A spokesperson for the European Union External Action Service said the EU is following developments closely. “We call on all concerned to act with responsibility and restraint and to refrain from actions that could lead to further escalation of violence. While recognising the right to peaceful demonstration, the European Union expects that they remain non-violent and avoid any incitement to violence. The European Union also calls upon authorities to respect the fundamental right to peaceful protest and proportionality in the use of force when defending its legitimate security interests, and to uphold its international commitments,” the statement said.

“We are concerned by the violent clashes witnessed in Kazakhstan in recent days and are following developments closely. We call for calm. Protests should be peaceful and law enforcement responses proportionate and in line with Kazakhstan’s international commitments. The UK encourages a peaceful resolution through engagement between the authorities and civil society,” a spokesperson for the UK Foreign, Commonwealth and Development Office said in a statement emailed to bne IntelliNews.

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BOOK REVIEW

Death of the Soviet Union – reassessing the causes of the Soviet demise

Clare Nuttall in Glasgow

Vladislav Zubok’s book ‘Collapse: the fall of the Soviet Union’ was years in the making, and it shows: this is a meticulously researched book examining the causes of the demise of the Soviet Union and challenging the frequently held view that the collapse was inevitable.

Zubok, now a professor of international history at the London School of Economics (LSE), was airborne at the moment the Soviet Union ceased to be, on a flight from the US to Moscow. In the years since then, he writes, the passing of time has tended to cause views on its demise to crystallise rather than become more considered. In the West, the fall of the Soviet Union has become almost universally seen as inevitable, while Russian views are polarised between those who feel they are well rid of the communist era, and those who look back with nostalgia.

The appointment of Mikhail Gorbachev as leader of the Communist Party in March 1985 was, as identified by Zubok, the critical turning point. He avoids the assumption that the Soviet Union was doomed, instead examining the choices by its new leader that led ultimately to its undoing. “Gorbachev lies at the centre of the puzzle,” he writes. He skilfully profiles Gorbachev and other key actors, notably Boris Yeltsin, illustrating the intense rivalry between the two.

Zubok identifies the five broad reasons seen as contributing to the fall of the Soviet Union, among them the US’ superiority in the Cold War, the policy of glasnost that discredited the communist ideology, the implosion of the Soviet economy, national independence movements and opposition to Gorbachev’s reforms from powerful Soviet elites. He argues that “none of these causes, when taken separately, could have destroyed the Soviet Union ... all these threads had converged in a kind of perfect storm, unleashed by the rule of Mikhail Gorbachev.”

The changes made by Gorbachev followed a decade and a half during which the Soviet leadership was aware of the need for reforms, yet resisted them. However, when Gorbachev did launch the long-overdue reforms, they were underpinned by ideas and designs that were “fatally outdated, economically flawed and led to the destruction of the existing economy and polity from within”, according to the author.

Specifically, he describes the leader’s move to dismantle the Communist Party apparatus as a “historic miscalculation”. Perestroika “exposed the Soviet Union to the demons of economic chaos, political populism, nationalism and more”. Having initiated these changes, Gorbachev was unable to control the “destructive forces” he had unleashed.

In particular, the book delves into the economic and financial issues behind the collapse, as shown by the massive injections of ruble liquidity leading to hyperinflation that rendered the population’s savings worthless. Indeed, by the time Ukraine departed from the Soviet Union, sometimes seen as the point after which it was unable to recover and reshape itself, the union was already in a state of financial collapse.

In this weighty yet readable tome Zubok draws on his interviews with people at the heart of events including Mikhail Gorbachev’s former aides and high-ranking western diplomats, as well as a huge range of archive materials and other sources. It’s this depth of research and lengthy consideration of events in the tumultuous year of 1991 that makes his book stand out from the many others that explore the collapse of the Soviet Union.

‘Collapse: the fall of the Soviet Union’ by Vladislav Zubok is published by Yale University Press.

“The appointment of Mikhail Gorbachev as leader of the Communist Party in March 1985 was, as identified by Zubok, the critical turning point”
Russian oil production up on last year in December, gas production in 2021 breaks multi-year high

CDU TEK has published Russia’s oil and gas production statistics for December 2021 that show oil output was well up on 2020 but still lagging well behind production in 2018 and 2019. The results also show that Russia ended 2021 producing more gas than at any time in the last four years, both in December and for the full year.

Russia’s gas output was also up 4% year on year in December to 69bn cubic metres, CDU TEK reports. Gazprom increased production 4.9% y/y to 47.2 bcm. Novatek’s standalone production rose 4.5% y/y.

Poland’s CPI surges 8.6% y/y in December, the highest rate since November 2000

Polish CPI accelerated 0.9pp to 8.6% y/y in December, the highest rate since November 2000, the statistical office GUS said in a flash estimate on January 7.

Price growth continues uninterrupted with the flash reading 0.3pp above the forecast median. The December reading provides only more grounds for the National Bank of Poland (NBP) to keep on raising interest rates after four hikes in October-January.

Annual growth of Slovenia’s retail sales speeds up to 41% y/y in November

Slovenia’s retail sales soared by an annual 41% in November, accelerating from a 34.3% y/y growth in the previous month, the statistics office said.

Retail sales also grew compared to pre-pandemic November 2019, by 19.3%. The annual growth was primarily a consequence of the increase in retail trade with automotive fuel up by 79.4%.

Georgian FDI remains subdued

Foreign direct investment to Georgia slightly recovered from the subdued levels in 2020, rising close to $300mn in the second and the third quarters of 2021, but, overall, it remained at a comparatively low level of 3.6% of GDP ($594mn) in the rolling four quarters as of the end of September.

Detailed data revealed by the statistics office Geostat suggest that a large part of the FDI was actually retained earnings generated by the two major banks TBC and Bank of Georgia, controlled by UK-registered holdings. In the second quarter alone, the overall FDI was revised upwards by $64mn as the result of supplementary profits reported by “the financial sector”.

In 2019, before the crisis, the FDI reached $1.34bn, or 7% of GDP.
PMI data shows Turkey’s manufacturing hit by intense inflationary pressure in December

bne IntelliNews

Turkey’s intense inflationary pressures weighed on the country’s manufacturing sector in December, purchasing managers’ index (PMI) survey data from the Istanbul Chamber of Industry and IHS Markit has shown.

Andrew Harker, economics director at IHS Markit, said: "Cost pressures hampered operations across the Turkish manufacturing sector in December. Record rises in input costs and selling prices deterred customers from committing to new orders, led manufacturers themselves to scale back purchasing and further disrupted supply chains. Alongside the potential issues caused by the emergence of the Omicron variant of the COVID-19 pandemic, the sector begins 2022 in a challenging position."

Turkish manufacturing firms, however, reported a further increase in staffing levels during December, meaning the headline PMI for their sector remained above the 50.0 no-change mark in the month, ticking up slightly to 52.1 from 52.0 in November.

IHS Markit said: "Continued job creation was one of the factors behind the latest improvement in business conditions. Employment rose for the nineteenth successive month, and at a solid pace that was the fastest since August. Rising staffing levels were often linked to efforts to expand capacity."

Operations ‘hampered’

It added: "Other indices from the latest survey painted a less positive picture, however, with operations often hampered by steep inflationary pressures. "Input costs rose at the sharpest pace since the survey began in mid-2005, with the rate of inflation surpassing the previous record from September 2018. "Firms indicated that lira depreciation was the principal factor pushing up cost burdens. In turn, manufacturers also raised their selling prices at a record pace. Rising prices often deterred customers, resulting in a third successive moderation of total new orders. This was despite new export business continuing to expand amid improving international demand."

Production was scaled back in December, following a marginal rise in November, IHS Markit also noted, adding: "Again, price pressures were mentioned as a factor behind the slowdown. Firms also moderated their purchasing activity and reduced holdings of both inputs and finished goods due to efforts to contain costs and respond to softer demand conditions. There were again widespread difficulties in sourcing inputs as suppliers’ delivery times lengthened to the second-greatest extent on record. "According to respondents, delays reflected difficulties obtaining raw materials, in some cases due to fluctuating prices, as well as issues with transportation and particular problems securing goods from abroad."

Historical overview

Source: Istanbul Chamber of Industry, IHS Markit.
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