



HOUSE OF LORDS

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THE EU AND RUSSIA

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Witnesses: His Excellency Andrii Kuzmenko

Professor Sergei Guriev

Members present

Lord Tugendhat (Chairman)
Baroness Billingham
Baroness Bonham-Carter of Yarnbury
Baroness Coussins
Lord Foulkes of Cumnock
Baroness Henig
Lord Jopling
Lord MacLennan of Rogart
Lord Radice
Earl of Sandwich
Lord Trimble
Baroness Young of Hornsey

Examination of Witness

Ambassador Andrii Kuzmenko, Ukrainian Acting Ambassador to the UK

Q67 The Chairman: Ambassador, thank you very much for coming before this Committee. It is very good of you to do so. We are very interested in what you have to say as the representative of the Ukrainian Government in London. As I think you appreciate, this is a formal, on-the-record evidence session. We will ask you questions, and if you feel at the end of this session that we have not covered everything or that on reflection there are further points you wish to make, please submit written evidence. If we feel that we have not reached the end of the road, as it were, we may also ask you for written evidence. If, as our inquiry progresses and you read the evidence of other people, you feel that you would like to comment on what other people say, we look forward to hearing from you.

As we agreed before you came in, I will kick off with the first question, and if you then turn it into a statement, that is fine. Could I please ask you first of all to update the Committee on recent events in eastern Ukraine and what you think the next steps are to resolve the conflict? What, in your view, is President Putin's strategic plan for Ukraine? You are not his spokesman, but I am sure that you have a view on what President Putin is hoping to achieve. On that basis, what do you think the proper relationship should be between the two sides, Ukraine on the one hand and Russia on the other? Over to you.

Ambassador Andrii Kuzmenko: My Lords, I am really honoured to be here today. This is a great event and I hope that the information you will receive will be relevant and instrumental for you in your work. A very brief background, if I may. After the Revolution of Dignity, we had the annexation of Crimea by the Russians. Afterwards, in just weeks the turbulent events started in the eastern part of Ukraine, namely in the Donetsk and Lugansk regions, inspired, fed, paid and equipped by the Russians. We unfortunately failed to solve the issue by political means since the opposite side was acting under conditions of hybrid war, with the methods of a terrorist organisation equipped with modern armaments received from the Russian Federation.

We started the military counteraction and we were quite successful in liberating our territory from the occupiers—from the Russian mercenaries and the Russian military specialists, let us say—until the end of August, when, understanding that Ukraine would soon be very successful and would clean up the territories, the Russians sent their regular troops. It was the feet of Russian soldiers directly on Ukrainian territory. That was proved by the international organisations—by NATO, by the EU, by the OSCE—by the means of monitoring.

At that stage, we decided to find a solution by diplomatic means. The negotiations of the so-called contact group were held in Minsk in Belarus. We actually met more than once in this group. Two documents were signed—the Minsk agreement and the Minsk protocol—with a huge set of political and military measures based upon the peaceful plan of President Poroshenko. It was done to avoid casualties among civilians; to avoid further destruction and devastation of the infrastructure of the territory, which is outside Ukrainian control now, unfortunately; and to help start a peaceful settlement under democratic, transparent European procedures in the territory of the occupied regions.

I would like to say immediately that Putin's proposed term "Novorossiia", or "New Russia", which was waved on the slogans, has nothing to do with the reality, since the occupied territories are not even the full Lugansk and Donetsk oblasts: they are just a small part of these territories—up to 3% of the Ukrainian national territory. That is why all their attempts to show this as the failure of the Ukrainian state are nothing but propaganda, since we have successfully stopped the Russian military machine, the terrorists and the Russian mercenaries. This is the main result of what we have now.

Later on I will tell you in detail about the Minsk agreement and the state of play, since this is the key element in the peaceful settlement, but I will just respond to your direct question: what are the next steps? Today and tomorrow there will be meetings in Milan. The President of Ukraine, Mr Poroshenko, will meet world leaders and there will be a multilateral meeting with Mr Putin under the presidency of Italian Prime Minister Renzi. We Ukrainians are using each and every possibility for making dialogue with the Russians. Unfortunately, the promises we received are far from being implemented. In recent days, there was information that the Russians had started the withdrawal of their troops from the territories adjacent to the Ukrainian border and from Ukrainian territory itself. Unfortunately, under the official NATO statement of General Bradshaw, we could not confirm finally whether this was a withdrawal or a rotation of their people.

As far as Mr Putin is concerned, it is very difficult to understand what this leader of this big country had in mind thinking about the annexation of Ukrainian territory and the direct military aggression. We have not formally declared war, but under the assessment of the Russian non-governmental organisation Cargo 200—this is the military nickname that is used for military victims—up to 4,000 military personnel on the Russian side have been killed in military action in the territory of Ukraine. This country is doing its best to hide this information from society by way of secret funerals and the prosecution of people who are trying to tell the truth about it, including the beating of the British correspondent from the BBC who was trying to make a documentary about it. Crimea was definitely only a small part of the big plan. Apparently, although we cannot guarantee it, Mr Putin's best idea and intention—and this was proved later more than once by the statements by his narrow circle—was to reincarnate the Russian empire at least as the border of the former Soviet Union. For that reason Ukraine is definitely something the Kremlin needed. Even in terms of logistics it was necessary after the Crimean annexation if not to take all the territory of Ukraine then to have a ground corridor to that, with further probable plans for Transnistria and entrance to certain Balkan country territories. This is the perception, the understanding and the result of the analysis of the logic of the events we see.

Now, as I said, the Ukrainian army and Ukrainian volunteers have stopped this military machine and 70% of the territory of Donetsk and Lugansk oblasts are free: just 30% of the territories are under their control.

The Chairman: Ambassador, I am getting a little worried, because there are lots of other questions.

Ambassador Andrii Kuzmenko: Yes. Sorry.

Q68 Lord Maclennan of Rogart: Thank you, Ambassador. The lead-up to the crisis in Ukraine and Crimea has provoked a letter, published in the Financial Times, from the ambassador of Russia to the United Kingdom, Dr Yakovenko, suggesting that they object in the first place to “the secretive method of the EU in dealing with Ukraine”. Could you give us some indication of what steps might have been taken by the EU that could have helped to ease that tension? When did the Russians raise their concerns about the Association Agreement? Do you think that relations during the period of negotiation on the Association Agreement could have been better handled?

Ambassador Andrii Kuzmenko: Thank you for your question. First of all, it is an absolutely disgusting statement that we were making our business with the EU in secret. Everything was open for the public, for all the countries; all the results and all the reports were in the media. It was the decision of a sovereign state to isolate, to be a part of Europe and to choose a

European future. No one country, no one leader, has the right to stop or to neglect that decision taken in a democratic way.

The first concerns from the Russian side started when they realised that the signing of the Association Agreement was real. The summit in Vilnius was the expected and planned date for the signing of that document, but a lot was done to prevent Ukraine from signing before the tragic event that we were talking about and that we will be talking about later on. There were a number of different “wars”—a customs war, a gas war, a milk war, a meat war, cheese war, a chocolate war—and the Russians started against Ukraine with the solemn purpose of pursuing us to postpone and then refuse European integration. During the time of Mr Yanukovich, they succeeded in principle at the administrative and the governmental level, since the nation was not in agreement. That was the reason for the protests, since no one could deprive the nation of its sovereign choice.

What further steps have we taken? We have ratified the Association Agreement. Up to half a dozen European nations have already also ratified this document, in spite of the enormous pressure of the Russians. We and the European Union clearly stated that the text of the Association Agreement will not be changed, since this document is already signed. Some of the states have ratified it, and this is the sovereign will of Ukraine on the one hand and the European Union countries on the other. For Ukraine, the Association Agreement is a road map of reforms. Despite this difficult time of war, we are very keen on its implementation and we are doing our best to adopt legislation, make economic reforms and fight corruption. The scope of obligations in this agreement is equal somehow to those that were set forth in the agreements for future membership of certain countries in the Baltic region and central Europe at the beginning of the 2000s. For us it is important, and we will go on this way.

Q69 Lord Jopling: Ambassador, a good deal of negotiation goes on through the trilateral process. I wondered, to begin with, whether you would just like to tell us briefly how satisfied you are with the trilateral process. Do you think it is legitimate? Do you think it is a good way of dealing with the problems? Having said that, the implementation of the Deep and Comprehensive Free Trade Agreement has been postponed, as you will know, until December of next year. Do you think that is sensible? President Barroso—and I quote some of his words, if I can find them—has said that further consultations would be sensible to address concerns raised by Russia as to the “perceived negative impacts on the Russian economy” of the DCFTA. Do you think there is ground there? Do you think it might be possible to make progress by trying to address negative impacts on the Russian economy?

Ambassador Andrii Kuzmenko: My Lord, thank you very much for your question. First of all, we are ready to address all the concerns of the Russian neighbours. We are listening to them and we are trying to do our best to provide them with full information. The trilateral process is a very good instrument to explain to the Russians that the majority of their negative expectations, worries and concerns about the Association Agreement are groundless. Moreover, Russia will receive a lot of positives when Ukraine starts the full-scale implementation of the Association Agreement, including the FTA, since it will be the precondition for deepening ties between the Russian economy and the economy of the European Union with the use of Ukrainian partners, Ukrainian possibilities and the traditional ties that we have.

With regard to the decision to postpone the FTA, the Russians are reluctant to hear us and still pose their concerns, but that was the compromise reached in the trilateral format in deep consultations with the European side also, and we understand that these should calm them down. It was a compromise, unfortunately. We are living where we are. However, one more time, all the negative expectations of the Russians, which mainly have a propaganda nature,

are groundless. The EU economy is much stronger than the economy of Ukraine and the ties of the Russian economy with the united economy of the European Union will be nothing but beneficial, first of all, for the Russian side. It is obvious.

Lord Jopling: You say that the Russian concerns are “groundless”—that was the phrase you used—but Barroso has suggested that it would be useful to try to find ways of dealing with the Russians’ perceived negative impacts. Do you think that is a sensible approach?

Ambassador Andrii Kuzmenko: First of all, to my knowledge at least, we have not received the full picture of possible negative impact to the Russian economy. There are a lot of slogans and a lot of speculation on that issue. This is our part of the deal: to explain, to provide them with the information, and, as in the case of the DCFTA, even to make certain compromises. The soonest entering into force of the Association Agreement, including the DCFTA, will be just for the benefit of all the countries of the continent, including Russia.

Lord Jopling: However, you say that you have not yet received the Russian concerns. If you have not received them, surely when you do it is worth seeing what can be done to alleviate them.

Ambassador Andrii Kuzmenko: My Lord, we have this trilateral mechanism. The consultations are under way. That mechanism is a platform to meet those concerns—to explain to the Russians the grounds of our actions and the groundlessness of their concern. Moreover, it is our sovereign right to choose the way of our further development, and it is the obligation of a European country to keep a tie with all its partners and to try to do its best in economic terms.

Q70 Baroness Coussins: Good morning. What retaliatory steps has Russia taken against the Ukraine economy? Could you describe those? Also, could you say what your assessment is of the Commission’s efforts to hold Russia to WTO commitments through the dispute-settlement process? Do you think that these efforts are likely to change Russian behaviour at all?

Ambassador Andrii Kuzmenko: Thank you for your question. I will start with probably the easiest and shortest part. The Commission’s efforts at WTO dispute settlement are useful as part of wider long-term comprehensive measures. These measures will certainly bring results in a couple of years, but we should understand that we need results right now. The history of the economic trade war is a very long one, and this continues, which is most sensible for us. We have had our gas supply from Russia cut off. This is very big trouble for an economy that historically and traditionally depended 100% on Russian gas and the Russian energy supply. Meanwhile, we continue to pump the gas for European suppliers and customers, and we are doing that reliably on a daily basis despite the fact that we are deprived of the use of that gas.

In other economic measures, there is a long list of sanctions targeted against Ukrainian goods—Ukrainian agriculture goods first of all, which are a traditional component of the Russian food market. We are seeking other markets and other customers for our goods, and in principle we have succeeded in changing the balance and in finding alternative markets for them.

Q71 Lord Trimble: I want to turn to the question of Crimea and the plans for settlement of Crimea’s political status. Do you think that the EU’s policy maintaining the principle of non-recognition is sustainable? How do you think this issue can be handled?

Ambassador Andrii Kuzmenko: My Lord, thank you for your question. For us and for the European states, the political status of Crimea is settled. This is a temporarily occupied

territory of Ukraine. The Russian annexation of Crimea is not recognised and we strongly believe that it will never be recognised. We are grateful to the United Kingdom, the European Union and our partners and friends for their consistent and constructive support of Ukraine in this issue, but we should also think about the population of the Crimean peninsula, since the annexation brought to the territory a lot of controversial and messy—if I may say—processes and events. First of all, this territory has started to face massive human rights violations based on the violation of the national rights of the Crimean Tatars and Ukrainians living there. In fact, the Ukrainian language is mainly prohibited there, despite the political declarations that it will be the sole language. We are witnessing fires of Ukrainian books in the courtyards of schools. We are witnessing the banning of Crimean Tatars' national or political body, the Mejlis. We are witnessing the kidnapping and even killing of Crimean Tatars, a nation that supports Ukraine and did not recognise the occupation. Meanwhile, winter is coming, but Crimea has no other electricity supplies except from the Ukrainian territory. It receives 75% of its electricity and 75% to 80% of its gas from Ukraine, as well as food. Traditionally Ukraine was the region's breadbasket. Now the shelves at the shops are semi-empty. There is no variety of goods, just basic ones. Ukraine still supplies gas and water, which is more important, to Crimea, including natural gas, despite the shortage that we have, since we know that our people are living there and that sooner or later Crimea will be back to Ukraine.

The Chairman: You are continuing to supply it, are you?

Ambassador Andrii Kuzmenko: We are continuing to supply.

The Chairman: In what currency are you paid?

Ambassador Andrii Kuzmenko: There is not much information about the payments. It is difficult to say whether the obligations for payment of those gas, electricity and water bills are fulfilled. To my knowledge—I would like to emphasise “to my knowledge”—they are not up to date in paying and there are big arrears. However, that is to my knowledge.

The Chairman: You are continuing to supply gas and electricity.

Ambassador Andrii Kuzmenko: We are continuing to supply.

The Chairman: And the Russians are continuing to supply—

Ambassador Andrii Kuzmenko: The Russians have no technical means to supply.

The Chairman: No, but the Russians are continuing to supply gas to Ukraine.

Ambassador Andrii Kuzmenko: No.

The Chairman: Have the Russians cut off gas?

Ambassador Andrii Kuzmenko: As I said previously, the Russians cut off the gas supply to Ukraine in April or May. We are living on our own resources and we are living with the gas received from some European countries. Despite that, we still supply Crimea and we still supply Donetsk and Lugansk—territories that are outside our control—and, of course, they pay nothing.

Lord Trimble: With regard to those supplies to Donetsk, Lugansk and Crimea, are you still supplying at the same level as before these incidents occurred, or is the supply going at a lower level?

Ambassador Andrii Kuzmenko: It is difficult for me to respond on this issue. The level of supply is probably smaller, since a lot of enterprises, especially in the Donetsk and Lugansk regions, are stopped right now, but the population has gas, water and electricity—at least where the respective infrastructure objects have not been destroyed.

The Chairman: Are you still able to pursue the development of your onshore and offshore shale gas fields, or is the occupation of the Crimea putting a stop to that?

Ambassador Andrii Kuzmenko: My Lord, thank you for your question. We are still working in the western part of Ukraine on the deposits of shale gas. In the eastern part of Ukraine, by coincidence probably, the territories with deposits of shale gas were the very centre of the terrorist uprising, if I may say, but we did not cancel our plans. We are expecting a peaceful solution for the region and we hope it will continue later on.

Q72 Lord Foulkes of Cumnock: It is nice to see you, Ambassador. Imagine yourself sitting in Moscow rather than Kiev and looking from a Russian point of view. You have lost the Soviet Union. You see the former satellite countries joining the European Union. Then you see the European Union creeping further forward and taking in countries—or wanting to take in countries—that were part of the Soviet Union itself. You can see why they get nervous about their influence. Do you think that the European Union might review its Neighbourhood Policy—our Eastern Partnership programme? I keep asking this: do you think we should say, “Where is the eastern boundary of Europe?”. We have not defined it and there is an assumption that we can keep going on and on expanding into what I would think is Asia rather than Europe—at least, it is certainly not Europe. Maybe as far as Ukraine, Moldova and Georgia are concerned there could be joint collaborative arrangements between the European Union and Russia so that they are not part of Russia’s influence or our influence but we have a joint concern for them. Should we not review that in some way?

Ambassador Andrii Kuzmenko: Thank you for your question, my Lord. It is difficult to imagine that I am in Moscow, but coming back to the European Neighbourhood Policy, this is a rather powerful instrument, which helped to conclude the Association Agreements with Ukraine, Georgia and Moldova. This is the historical achievement; it proved its efficiency. It could also be a good framework for countries such as Belarus and Azerbaijan for their proximity to Europe. Of course, we—Ukraine—and other countries, like Moldova and Georgia, that have already signed Association Agreements are not a backyard of Russia, and we have our own sovereign rights. This is the issue to be solved and to be decided by the EU.

We would like to emphasise one more time that all their concerns, especially about the move of NATO towards Ukraine, are groundless. In fact, since 2010, Ukraine’s non-bloc and neutral status has been fixed at legislative level. Now we feel growing and stronger sentiments towards collective systems of defence, but this is not, of course, the Tashkent treaty.

Where is the border? For us it is clear enough that Ukraine is covered by the border of Europe. We are a European nation; we have a European destiny and a European future.

Lord Foulkes of Cumnock: I know it is difficult for you to put yourself in the shoes of a Russian, but can you see why they might be concerned that the influence of the European Union is extending? Maybe after Ukraine there would be ambitions to involve as members other countries further east, and that might be worrying them also.

Ambassador Andrii Kuzmenko: Now I will respond to your question about what I think should be done if I were in the Kremlin. All these worries and all these problems have arisen in Russia due to the economic and political weakness of that country. Now we are facing \$82 per barrel of Brent oil, which is a terrible fall-down for the Russian economy. If I were in the Kremlin, I would concentrate my attempts on modernising the economy, on the growth and modernisation of democratic institutions, and on civil society as a guarantor. All of Europe is leading; some countries are in the European Union, some countries are in NATO, and they do not have concerns since they have strong economies, strong democratic societies, and strong

institutions and civil society. Probably the reason for everything was just the lack of modern understanding of the processes in the world, and the decision to act in the 21st century with the instruments not even of the 20th century but the 19th century.

Q73 Baroness Henig: Good morning, Ambassador. Can I shift the focus slightly toward the Eurasian Economic Union and ask what, in Kiev's view, would be the best way for the members of the EU to structure a relationship between the EU and the Eurasian Economic Union? I take your point that you are not Russia's backyard; you are in a way a hinge between these two great arrangements. I wonder, therefore, how you would see this developing.

Ambassador Andrii Kuzmenko: Coming back to this Eurasian Union problem, this is the geopolitical project of President Putin. As a matter of fact, the relations within this Eurasian Union are the relations of one huge country supporting its smaller dependent countries in the interest of the big one. How do we develop relations between the EU and the Eurasian Union? In fact, it will be the relations between Russia and the EU mainly. It will not be the best idea to develop these relations against the situation that we have in Ukraine—and not only in Ukraine, given the tribalisation still in the territories of frozen conflicts where the Russians are trying to exert influence.

The Chairman: In the light of your answers to Lord Foulkes and Baroness Henig, could I ask you: does Ukraine have an ambition to join NATO?

Ambassador Andrii Kuzmenko: The Government have submitted to the Verkhovna Rada—to Parliament—a draft bill to annul the previous decision on non-bloc and neutral status. It is rather premature to speak about Ukrainian membership of NATO. We are close partners to the organisation and the only non-allied country taking part in all the missions of the alliance. Meanwhile, the sentiment among the Ukrainian population is growing, and some reliable polls already have demonstrated that up to 52% are in favour of joining NATO in the future; 34% are against, which is rather big; and the rest have not decided yet. But at this very moment, we are not pushing the issue of membership. It should be the decision of the nation, and at this moment it is premature to take it.

Lord Jopling: Ambassador, you might just like to reconsider the comment you made a moment ago. You were saying that Ukraine was the only non-aligned country that takes part in NATO activities.

Ambassador Andrii Kuzmenko: In all NATO activities. We have been involved in all the missions, including in Afghanistan.

Lord Jopling: I missed the word “all”. There are certainly others.

Q74 Earl of Sandwich: Mr Kuzmenko, coming back to Lord Foulkes' question to some extent, you will be aware that the Commission is about to appoint a new Commissioner for enlargement. In fact, this has now been confirmed. At the same time, there is a new policy from the President that we will not be having an enlargement policy. There is some contradiction in my mind about that. I would very much appreciate your view from the Ukraine point of view on what is the likely scenario in the European Union if we are moving back to consolidation instead of enlargement. This may have consequences for the association agreement itself and further delay the whole enterprise.

Ambassador Andrii Kuzmenko: First of all, the decision to move to consolidation versus enlargement falls within the direct responsibility of Brussels, and it is difficult for countries seeking association to command that. However, as in the case of NATO, we are not pushing

for membership now. We have signed and are keen to implement the Association Agreement. The fundamental project and programme for the reforms is a very important tool in the modernisation of Ukraine, and when the so-called criteria are reached there, we will probably bring up the issue of our possible membership. In fact, Mr Poroshenko, the President of Ukraine, stated that we should be ready economically, politically and democratically to submit the application for membership for the year 2020, but before that we will concentrate our efforts on modernising all the areas of our life. This is on the way. Despite the military conflict in certain territories of the Donetsk and Lugansk regions, we are very active in modernising the Ukrainian legislation. For example, just two days ago we passed a law on prosecution. This is a very long-standing issue, which the two previous Presidents failed to solve. We have adopted the package of anti-corruption law. It is very important for Ukrainian society. We have also adopted a long list of documents regarding the democratisation of our society. Among those is a law on lustration, which also helps us to clean up the Government and local authorities from the corrupted people who collaborated with the previous authorities to harm Ukraine.

Q75 Baroness Young of Hornsey: Ambassador, witnesses have told us that the EU should continue to engage with Russia. I am wondering what, from your point of view, the nature of that engagement should be. In what ways should the EU and member states engage with Russia? Do you think there needs to be a cooling-off period, given the recent turmoil? Do you think there are areas where the EU and Russia can have a really constructive dialogue?

Ambassador Andrii Kuzmenko: Dialogue is always better than countermeasures, but dialogue is possible only where the two sides are hearing the arguments and are trying to stick to the proposals and implement them. For the moment, vis-à-vis this situation in Ukraine, I think the best stance for the EU is a hard position vis-à-vis Russia—to continue the sanctions against Russia, which were not the kind of the remedy that we were happy to see. This was the means to stop the aggression against the Ukrainian territory. Now we see that these sanctions have started to work. They have had a calming effect on the Russian leadership, and it is probably not by chance that in the next few days we will have a meeting with Mr Putin in this format with the heads of the key EU states. This is probably the best way to deal with it. You, the European Union, should not, of course, leave Ukraine to deal with Russia alone. We need your economic and financial support, and we need your technical military support, which is very important for us since we are fighting not just for the territorial integrity or sovereignty of Ukraine but for the European values that we are adhering to. We are the only European country that has paid such a price just for its declared decision to become a future European state.

Baroness Young of Hornsey: You were saying that the sanctions are beginning to bite—to have an impact.

Ambassador Andrii Kuzmenko: Yes, they are.

Baroness Young of Hornsey: Do you not think there should be some form of dialogue that, as you say, requires all sides to participate? Do you not think there should be something alongside that? What should the nature of that be? What happens post-sanctions?

Ambassador Andrii Kuzmenko: It is very simple. In the negotiations with Russia about sanctions and tough economic and political co-operation, in our opinion the criteria have to be the full withdrawal of Russian troops from Ukrainian territory—including Crimea, which is Ukrainian—and the restoration of the previously existing order: *restitutio in integrum*, let us say. We will be ready and eager to co-operate with a friendly neighbouring country if that is the case, but the preconditions for that should be the restoration of the territorial integrity of

Ukraine, the total withdrawal of troops, and the end of its aggressive policy based upon imperialistic desires to create a new empire.

Q76 Lord Radice: We have been talking about your relationship with Russia. Do you still consider that the 1994 Budapest Memorandum, which was signed by Russia, Britain, the US and Ukraine, whereby, as you will remember, Ukraine gave up its nuclear weapons and in return the signatories agreed to respect the independence and sovereignty of the existing borders of Ukraine, still holds? Do you still believe in that agreement?

Ambassador Andrii Kuzmenko: We still consider this agreement to be valid. Besides, Russia has direct obligations under it, and we are waiting for it to implement them. Meanwhile, we are interested in upgrading this document, since it is mainly of a political nature. It was a declaration rather than a legally binding document. That was probably the reality of the time it was signed, but this document is valid. This is a ground for negotiations and the framework for a respective platform of assistance to Ukraine.

If I may, I will say just a few words about the peaceful plans of President Poroshenko and the situation in Donetsk and Lugansk oblasts. It will be a very brief few words. The Minsk protocol and Minsk agreement were signed, and they provided for a ceasefire that is, in fact, unilateral. During this ceasefire, we have lost up to 60 of our men and officers from the more than 1,300 cases of artillery, gun, mortar and rocket fire that we have witnessed. One of the separatist leaders was brave enough to praise this ceasefire since during it they took 33 Ukrainian small towns and villages. Those are the words of that separatist leader. Among the conditions of the ceasefire and the political settlement was control of the border, which is not the reality for the moment; it is outside any type of control. The OSCE mission, in its existing numbers and shape, is not enough to provide control at the border. Nearly every day we are witnessing the entrance into Ukraine of new technology and new military munitions for separatists.

With regard to the ceasefire, it was said by the so-called leaders of those terrorist organisations, the Donetsk People's Republic and the Lugansk People's Republic, that the fire is from the groupings that are not under their control, but it is clear enough that even in such cases the responsibility is with the side that supplies, feeds and pays, which is Russia.

The release of prisoners of war was agreed under the principle of "all by all". Unfortunately this has not happened. As of today, up to 500 Ukrainian prisoners of war are being held in extremely difficult, inhuman, conditions. We have witnessed torture; for example, one was brought back without a hand. It had been cut off, since there was a Ukrainian tattoo there. This is the kind of shameful war that we are seeing, but we still keep calm and carry on. We are responding to the fire only in cases where Ukrainian positions come under direct fire.

Moreover, the Russians kidnapped the Ukrainian pilot Nadiya Savchenko in their territory and, in the best tradition of the Brezhnev epoch, right now she is giving her evidence before a psychiatric commission. She is on trial in a court; she is accused of murders. The Ukrainian artist Sentsov from Crimea is also a prisoner of the Russian Federation, and this is more evidence of the human rights violations that we are witnessing and that we have to quit.

To conclude, Ukraine is motivated to restore its territorial integrity on the basis of democracy and human rights and the principles of European values. We are doing our best for that. It is a difficult time for us economically. I mentioned the gas supply being cut. It is very painful for us, but we are managing. This is the best proof that the thesis of some Moscow politologists about the failure of the state or the artificial state has failed. We are going towards our victory. We rely on our friends, allies and partners. We are seeking co-operation with Europe. We do not close the door for co-operation with Russia, but the precondition is

the restitutio in integrum of Ukrainian territory. Then we can start speaking. We also expect toughening sanctions, since this is the most reliable tool to halt the Russian aggression. If Ukraine fails, another country will appear in the near future, as in the case of Transnistria when it was Georgia, as in the case of Georgia when it was Crimea, and then, after the Crimean part of Ukraine, the Donetsk and Lugansk part of Ukraine. Who will be the next if we fail? That is why we will never fail.

The Chairman: Ambassador, thank you very much indeed. As I said at the beginning, if there is any additional point you wish to make or any further updates you wish to give us, please do, but I would like to thank you very much for the clarity of your answers. We realise this is a very difficult time for Ukraine and that you therefore are representing a country that is undergoing a great many problems. We are very grateful to you for coming before us.

Ambassador Andrii Kuzmenko: My Lord, thank you so much.

Examination of Witness

Professor Sergei Guriev, Professor of Economics, Sciences Po, Paris

Q77 The Chairman: Mr Guriev, thank you very much for coming before us. I do not think you were here at the start of the last session, so let me repeat what I said then. I think you are aware of it anyway. This is a formal session of the Committee. What you say, therefore, is going to be taken down and there will be a transcript. We will ask you questions, but if there is anything that you feel at the end of the session you would like to submit written evidence about or if you would like to enlarge your answers in written form, that is fine. We have an hour and we have another commitment after this, so we have to keep to the hour, so to the extent that you can keep your answers brief, it will enable more questions to be asked.

Let me pitch in with the first question, and if you then wish to add a statement to that, you are very welcome to do so. The EU and US sanctions are designed to put pressure on the Kremlin by raising the cost of capital for the Russian elite, and for the private and state-owned enterprises. Do you think this has been effective, or do you think that it also strengthens support for Mr Putin? It is quite possible that the sanctions are working economically but are strengthening him politically. I wonder whether you could give a judgment on those two sides of the equation.

Professor Guriev: Thank you very much for inviting me. I will not waste your time with long answers; I will try to be very short. I think that sanctions have worked. It is naive to expect sanctions of this calibre to have a dramatic impact in the immediate term, but they are working against the Russian economic future. They will make an impact in the next two or three years, making sure that the Russian economy is hit and the Russian Government budget suffers over the next two or three years. At the same time, the sanctions, as you rightly said, are used by the Government as a reason to intensify propaganda and to call Russians to rally around the flag. Some of the countersanctions introduced by the Russian Government themselves, such as a food embargo against the US, Europe and certain other countries, have also hurt Russian consumers and the Russian economy, but the power of the Russian government media as well as the censorship and political repression going on in today's Russia can convince Russians that even those sanctions should be blamed on the West as well. In that sense, yes, currently we see that the majority of the Russian public are convinced

that Russia is a besieged fortress and there is a reason to rally around the flag and pay the cost.

At the same time, sanctions have worked already in the way that they have managed to change the calculus of the Russian elite. Those who say that Russia neglected the cost of the sanctions fail to see that while Crimea was taken by Russia and became part of Russia very quickly—within days of the referendum held in Crimea—Donetsk and Lugansk, even after holding a referendum, have not become part of Russia. Moreover, the Russian Government, who started with the sentiment that Ukraine has had a fascist coup, is now talking to the Ukrainian Government and the newly elected President and perceives him to be a legitimate counterpart in their negotiations.

We also see a ceasefire (with all the problems around this ceasefire). We see that the number of casualties is going down. I would not say that Russia is going to give back Crimea any time soon. I also expect that Russia will continue to destabilise the east of Ukraine, and yet the Russian Government have changed their stance, in the sense that Donetsk and Lugansk are not parts of Russia like Crimea is.

Lord Trimble: You were commenting on the impact of the sanctions. Would you have any view on the effect, although coincidental, of the very sharp reduction in the price of oil? What effect will that have on the public finances of Russia as distinct from the economy?

Professor Guriev: This is a very good question. The short answer is that the price of oil will hit Russian public finances, and this effect will be strongly reinforced by the sanctions. The long answer is that the Russian budget for the next three years is based on the price of oil of \$100 per barrel. As you probably know, the price yesterday was more like \$85 and today it is more like \$83. Anything in the range of \$80 to \$85 per barrel directly implies that the Russian Government will face significant problems three years down the road. Not this year, not next year. The Russian Government has a Reserve Fund that now stands at 5% of GDP. There is another sovereign wealth fund—the so-called National Welfare Fund—which is also 5% of GDP but is already committed to infrastructure projects, to bailing out state banks and to helping companies that are suffering from the sanctions, so we should look only at the Reserve Fund. In that sense, the Russian Government is facing a problem.

The good news for the Russian economy is that the Russian Central Bank is committed to a floating exchange rate regime, so the rouble is taking the hit, which helps the Russian Government budget, as Russian government spending is denominated in roubles while half of the Russian budget is coming in oil and gas revenues. The weakening of the rouble will help the Russian Government to balance the books. However, that does not solve all the Government's problems. Why? Because a cheaper rouble also means lower purchasing power for Russian consumers. We will see a decrease in the living standards of the Russian public, and the Russian Government will have to come up with certain—probably non-economic—solutions to convince Russians, as we discussed in the first question, that they are suffering economically for a good cause. How the Russian Government is going to address that is very hard to predict. If this year's experience teaches us any lessons, we should expect more propaganda, more repression and maybe even further foreign policy adventures.

Lord Radice: You said “further adventures”. What do you have in mind?

Professor Guriev: There are many Russians around the world, and Mr Putin has declared that he wants to protect Russians. Living in Paris, I am safer than you living in London. Paris has few Russians to protect; London has many Russians to protect. Seriously, I do not know. Nobody expected what happened this year, and the next steps may be as unexpected.

Lord Radice: You were not thinking of the Baltic states or anything like that.

Professor Guriev: Many things were impossible before. I would say that many things that were impossible before are now possible. I would not say the probability is high, but if you asked me a year ago I would have said it would be impossible.

Lord Jopling: But you think that it is possible despite Article 5 of the NATO agreement.

Professor Guriev: We cannot rule out the following scenario. Even if there are NATO soldiers—non-Baltic-state soldiers—on the ground in the Baltic states but not in every town of the Baltic states, if Russian troops move in and occupy part of the Baltic states' territory, we are not sure that NATO soldiers will shoot at Russian soldiers. There will be further negotiations and sanctions. This is the scenario that some people in Russia would consider. As Mr Putin reminded us yesterday, Russia is a nuclear power and hostilities with regard to a nuclear power may be problematic.

Q78 Lord Radice: You are an expert, are you not, on the relationship, and particularly the economic relationship, between the EU and Ukraine? The EU has committed €11.5 billion to support Ukraine. Is that enough? Are they delivering it? What do you think?

Professor Guriev: I am much less informed on the extent to which the funds are being disbursed and used. Ukraine is in a desperate economic situation; €11.5 billion is a substantial amount of money, something like 6% or 7% of Ukrainian GDP, which is a lot of money for any country. A lot more will be clear when the next Parliament is formed after the elections, which Government is shaped and what reform programme will be put together. It is crucial that the Ukrainian economy succeeds, because disillusionment in economic reforms may be very quick and may result in reversal. We understand that it is not in the interests of the current Russian Government to have Ukraine succeeding on this trajectory and we should expect all kinds of actions from the Russian side to undermine this process. In that sense, I expect that in a normal situation, this package would probably be enough. If the EU wants to see an independent, democratic and prosperous Ukraine, I think the EU should prepare to think about further programmes of support in Ukraine. If Ukraine follows the course that it has announced—that it wants to become a part of Europe, broadly speaking—I think that is completely possible, but it faces a very powerful enemy for whom the stakes are very high. A successful Ukraine free of corruption is a big challenge to the regime in Moscow.

Lord Foulkes of Cumnock: I would like to go back very quickly to sanctions. You mentioned the large number of Russians here in London. Is there scope for more effective sanctions because of that?

Professor Guriev: The value and the advantage of the West is that the West sticks to its own values and laws. That is why I would always advise western governments to take the high road, as they would say, and not retaliate against family members. But if the UK enforced the Bribery Act 2010, that would already be a major step forward against people who make foreign-policy decisions in Russia. There are many Russians who live in London who may have benefitted from corruption in Russia. I do not want to mention names because I do not have evidence in front of me. In private I can share certain observations. I have journalist friends and certain experts who have tried to investigate certain things, and they suggest that there are certain people living in London who are very important in Russia and for the Russian regime who could have suffered from serious investigation under the Bribery Act.

Baroness Billingham: Since the EU committed the, as you say, enormous sum, comparatively, of €11.5 billion, the positions of the economies in the EU themselves have weakened. What sort of effect is this going to have in the future? Do you think there is any question of reneging, or do you think that Ukraine's future is rather bleak?

Professor Guriev: That is a good question. Eventually it is for the voters of the member states, and I guess for the European Parliament, to decide on the priorities of the European Union and of the member states. The European economy is not in good shape, and sanctions against Russia and even countersanctions by Russia, although they have not had a dramatic effect, have had a negative effect on European growth perspectives. The sum of €11.5 billion is a huge sum for Ukraine; it is not a huge sum for Europe, but coming from France I see that every additional billion matters. Every additional billion may cost votes in a critical electoral district. We have seen that France is continuing with delivering battleships to Russia. France continues and suspends; every week brings different news, but it talks about delivering the battleships to Russia, with an amount at stake of about €1 billion. We see that every billion matters, exactly because we are talking about jobs and votes.

Q79 Lord Maclennan of Rogart: I would like to ask a historical question and a question about the present. The historical question is: do you believe that the EU could have assisted Russian economic development over the last 20 years? Did we falter or fail in that respect? The present question is: would a contribution to the strengthening of the economic position of Russia be a significant contributor to the resolution of the political questions? Could we do it? What could we do if we were to attempt it?

Professor Guriev: It is very hard to speculate about what would have happened if the EU had done something else. It was a disappointment in Russia in the 1990s that the West did not help as much as it could or should have done. A Marshall-Plan-like initiative would probably have made a difference. It is hard to judge now. It is difficult to say how that would change the probability of a Government like today's coming to power, but, yes, it was unfortunate that the EU did not commit more substantial resources to making sure that the economic shock of the 1990s was somehow mitigated.

To what extent Russia was prepared to co-operate with the EU is also not clear. Russia faced a major existential crisis, in the sense that, seeing the empire falling apart, Russia had a problem of identity, and at every moment of those last 20 years there would always be a political force that would be nostalgic about Soviet times, and this political force would always get a certain support from the Russian public. There was also an opportunity not just in the 1990s but in the 2000s, when Mr Putin was open to co-operation with the West. We saw some of that happening, for example, in co-operation with the US on the war on terror, especially in Afghanistan. We also saw some opportunities in the later 2000s.

At the end of the day, Russian political development is the business of Russia—it is the business of Russian voters. Eventually, Europe has promised and has offered “four common spaces”—integration of everything but institutions. In the later 2000s, Europe suggested the Partnership for Modernisation. That was not really happening. European foreign-policymakers apparently were busy with other things, which is understandable. Unfortunately, it is not the hostilities that insult the Russian Government but the neglect. That was also very clear in the mid-2000s, when the focus of US foreign policy was shifted elsewhere. For Russia, being a post-imperial country, being treated as a non-entity—as a non-important player—is an insult. If the EU in whatever capacity had been more active just in talking to the Russian Government, that could have created more space for dialogue. At the end of the day, all these things are speculations. The EU has not done anything illegitimate; if anything, there was an unfortunate lack of energy in engaging Russia. But all the offers were on the table and eventually it was, I guess, Russia's choice not to take them.

Q80 Baroness Henig: You have already given us examples of how economic issues have influenced the foreign policy of President Putin—and, indeed, the close linkages between

economic and political considerations. In the light of this, what is your assessment of President Putin's strategic aims in the European neighbourhood?

Professor Guriev: We do not really know what Mr Putin thinks and wants. There is a theory that suggests that he wants to restore a certain kind of "Great Russia", which would include what is the eastern neighbourhood for Europe (but for Russia, it would be the western neighbourhood). We all have heard then-President Medvedev saying that these countries are part of Russia's sphere of privileged interest. I have heard very recently advisers to Mr Putin saying that neighbouring countries will have limited sovereignty whether they want it or not. That may be a strategic goal.

There is another theory that suggests that the main goal of a regime like this is survival. Under the previous social compact, the public was happy with this Government because they delivered economic growth, even though the public understood that the Government was not democratic and was actually corrupt; the public still tolerated and actually supported this Government because economic growth was out there and everybody benefitted from it. This social compact is gone. The Russian economy is at best stagnating.

To offer a new source of legitimacy, the regime needs non-economic solutions. Bringing new countries into the sphere of interest, showing that Russia is an important country, showing there are greater things—than GDP per capita or economic growth or mortgages—tools for the regime to gain legitimacy and popularity and survive.

These two theories produce the same empirical predictions. It is very hard, judging by what we observe, to see whether Mr Putin is opportunistic or imperialistic. We do not know.

Q81 Lord Jopling: Let us turn back to Ukraine. President Putin has said that a Deep and Comprehensive Free Trade Agreement between the European Union and Ukraine would impact existing free trade agreements between Russia and Ukraine. How legitimate is that claim? Do you think that the European Union's regulatory and technical standards could have a detrimental effect on Russian trade with neighbouring countries?

Turning from Ukraine over to the proposed Eurasian Economic Union, we have been told that that is incompatible with the DCFTA. Do you think that is a legitimate argument? Do you think that the European Union and the Eurasian Economic Union can exist and co-operate together? If so, how might that be done?

Professor Guriev: It is a complicated question. I would just give one simple answer with an example. Russia's statement that a free trade area between Russia and Ukraine is not compatible with DCFTA is false. Canada is part of a free trade area with the US; Canada just negotiated a free trade agreement with the EU. There is nothing wrong with being a member of free trade areas with different partners. To what extent the DCFTA would be in the interests or against the interests of Russia is hard to judge. For certain interest groups in Russia, Ukraine joining the DCFTA would represent a problem; for certain businesses, more competition from European goods in Ukraine and Europe being a destination for Ukrainian export goods creates competition and therefore a cost. In the long run—and I think Mr Putin has said this many times himself—Russia is interested in a prosperous Ukraine, and it is in Russia's national interest to have more trade and more growth in Ukraine. I fully subscribe to this view. Is the Eurasian Economic Union incompatible with the DCFTA? Of course not, exactly because of this issue. To what extent does a Eurasian Economic Union—or Customs Union, as it used to be called—want Ukraine to be part of it? We have seen and heard that Mr Putin himself and his Government always inviting Ukraine to join them and it was always an ambition to have not just Belarus, Kazakhstan and Armenia but also Ukraine. Compared

with Belarus, Kazakhstan and Armenia together, Ukraine is a big market. Currently, as it stands, the Customs Union represents a political benefit for Russia, but it is not a strong economic benefit. It benefits Belarus and Kazakhstan, which gain access to the large Russian market, but not Russia. For Russia, Ukraine joining the Customs Union would justify the creation of the Customs Union.

Q82 Baroness Coussins: Good morning. We have heard from earlier witnesses to our inquiry that the EU is being, shall we say, less than diligent in observing and enforcing its own anti-corruption and anti-money-laundering legislation. I wonder what your assessment of that is. Also, what is your assessment of how the UK compares with other EU member states in this regard? Do you think there might even be a role for the UK in gold-plating EU legislation?

Professor Guriev: The EU and the UK could have done a much better job. For example, right now there are many people on the sanctions lists who have assets abroad, which they own through chains of companies. Hearing about the intelligence capacities of the US but also of Europe, many people in the world are surprised that these things are not tracked down. At the moment, the West has a lot of other things to care about—it probably does not have resources to commit to investigating those things—but it is surprising that this is not happening. Again, I will not mention any names in public—I do not want to make statements that I do not have immediate evidence on—but there are many rumours that certain members of UK and London-based establishments have been involved in corruption and money-laundering. Should the UK gold-plate EU legislation? Yes. It is in this particular area we see exactly this issue: where many people who are connected to the Russian Government live in the UK, have assets in the UK and do business in the UK. It is up to the UK to enforce its own laws. The laws in place are already quite strong; they should just be enforced. It is not about gold-plating legislation; it is about gold-plating enforcement practice.

Q83 Baroness Young of Hornsey: Following on from that, you have just mentioned that there are British business men—and women, presumably—who are involved in some of these corrupt practices. I would be interested to know your assessment of how large a problem that is and whether you think that somehow by engaging with Russian companies, particularly state companies, by sitting on boards and so on there is a sense in which those people are being co-opted into a Russian model of operation. Do you think that is the case? How would you judge the impact on the European business environment of doing business with Russia? Clearly you do think there is a role for the EU to uphold best practice of governance and regulation, so what more could they be doing to make sure they implement those regulations?

Professor Guriev: The view that Russia has managed to corrupt the Western elite is not correct. There are pro-Russian lobbyists in all European capitals, but mostly these are about the legitimate business interests of those companies. I strongly believe that companies' business, to the extent that they stick to the existing law, is to make money for their shareholders. This is what these companies do. This is why they ask for the removal of sanctions and for continued trade and investment with Russia. It is the job of politicians and law-enforcement authorities in European countries to enforce the existing laws and, if need be, to prosecute the companies that violate those laws. That has happened in the past. Certain western companies have been prosecuted for giving bribes to Russian government officials. Even in those cases, I should say, the Russian Government has not investigated those officials; these officials are doing very well, even though there are European Court decisions establishing the facts of bribery and corruption.

As for sitting on the boards of state companies, I would say that the number of cases is actually now very limited. Certain people, because of sanctions, because of the Ukrainian war and because of various issues related to integrity and the environment in those state companies, have quit the boards. In that sense, I would not overestimate the threat of the Western elite being corrupted by the Russian regime.

There are rumours that the Russian Government funds certain extreme parties in the European Union. I have not seen any evidence. Investigating this is extremely important and, if this comes out and these parties are damaged by that, I think that would be the best thing ever that Mr Putin has done for Europe.

However, generally I do not see any tangible evidence that the European elite is corrupted by the Russian regime. It is unfortunate that investigations are not as strict as they could have been. They should be stricter; there should be more resources devoted to investigations, but I do not see major political forces, especially those that run European countries, being corrupted.

The Chairman: You said earlier, if I heard you correctly, that you believe that companies are motivated by the interests of their shareholders—or, if you like, by earning profits—which is classical capitalist doctrine, but do you think that also applies to Russian companies? Are Russian companies not an instrument of the state rather than an instrument of their shareholders?

Professor Guriev: Generally I would say that state companies occasionally—and recently more often than not—follow orders of the Government. If the Government ask them to take decisions that are against shareholders’ interests but in the interests of the Government, state companies do that.

There are different kinds of state companies. Certain state companies have strong political connections with high-level officials, and only the very high-level officials are able to ask them to do something against their interests but in the interests of the political process within Russia. Certain companies are less politically connected and can be bossed around by low-level officials. However, in general, state companies are not independent of the Government and in many cases make decisions that a normal business, maximising shareholder value, would not. I can give you examples but probably in private.

Q84 Baroness Bonham-Carter of Yarnbury: There are a number of outstanding disputes between the EU and Russia at the WTO. Is the process to hold Russia to her WTO commitments effective and, indeed, is it a good process to be pursuing? Are they likely to change Russia’s behaviour in any way?

Professor Guriev: If we go back to the first disputes around imports of cars and so-called “utilisation duty”, Russia did not expect the extent to which the WTO is an effective mechanism. The WTO does not act quickly, but there is a certain degree of predictability about WTO dispute-settlement mechanisms. What Russia did was certainly against WTO rules and within months it was clear that the WTO would rule against Russia, and Russia withdrew. Well, it did not completely withdraw, but it reintroduced this utilisation duty on Russian carmakers as well.

Baroness Bonham-Carter of Yarnbury: So, it did change its behaviour.

Professor Guriev: It did change its behaviour; it complied with WTO rules, even without going all the way through WTO procedures, which would probably take a year and a half or two years. What is going on now compared with other things is completely minor. People ask questions like, “If Russia is not invited to the G8 or the G20, would that change Russian

behaviour?”. This is completely second or third order of magnitude compared with other things that are going on: sanctions, the oil price, war. These things are of a different order of magnitude. Would it help to reverse the Russian food embargo if Poland or the EU went to the WTO and said it is illegal? Such a decision would probably be important, but I can see that Russia can blatantly violate the WTO rules in this current political and economic climate. Is the embargo against the EU, Australia, Norway and the United States illegal by WTO rules? Yes.

Baroness Bonham-Carter of Yarnbury: What about the Lithuanian ban? Is that still in place?

Professor Guriev: Of that I am not sure. Some of the bans Russia has introduced were based on the pretext of phytosanitary controls, but that is a completely different story compared with the food embargo that was introduced in August. This is a clear violation of WTO rules. Russia comes out with a simple decision saying, “From these countries we will not import food – but from those we will”, which is exactly against the multilateral nature of the WTO. As I said, I expect Russia is just violating WTO rules. After the dispute-settlement mechanism rules that it is wrong, Russia will continue to violate the rules, and then Russia will just accept further trade sanctions imposed by WTO members.

Will Russia be kicked out of the WTO? I do not think so. There are always a few countries that would vote for Russia, and a consensus organisation cannot kick out anybody. I think even Russia voting for itself staying in the WTO will be enough for it to stay in the WTO, because it is a consensus organisation.

Q85 Baroness Billingham: My question follows on from that of my colleague here. Trade is a significant aspect of the EU-Russian relationship. However, deep trade relations have not led to good political relations. Could the EU do more to improve our trade relations? Should the EU have better economic relations and perhaps outline a set of rules and criteria to govern our trade relations with Russia?

Professor Guriev: Trade is important for economic development and growth. Interdependence in economic relations eventually raises the cost of political conflict. Mr Putin has always understood that. Economic interdependence, especially energy interdependence, was always on the agenda of Mr Putin’s relations with the EU; it was actually the main item of the 2006 G8 summit that Mr Putin hosted. Why does that not work? First, it did work in the past: trade has made relations better. Relations could have been worse. Trade has made relations better than they could have been otherwise. Secondly, even though trade raises the cost of political conflict, we see leaders that still are happy to take this cost.

Baroness Billingham: Does not President Putin have a number of aces still in his hand that make him stronger and able to take a cavalier approach to these negotiations and relations? He is shrugging and saying, “Do what you like”.

Professor Guriev: I think the situation is quite the opposite. The Soviet Union was isolated and could do many things. It would have been very hard to threaten the Soviet Union with the sanctions that Russia is facing now. The same is now true of North Korea. What could we do to North Korea? For the Russian Government and for Russian consumers, these sanctions are painful. Even though some people say that Mr Putin can do whatever he wants, he is in a very unfortunate situation—him personally and his regime as well—exactly because of the reasons I mentioned at the beginning. I do not see an exit option for today’s Government. I do not see how, unless the oil price goes back to \$140, this Government will be able to break even. In that sense, I am very sorry for the people running Russia now,

especially for Mr Putin, because I do not see how they can get out of this. In the short run, they can enjoy spending the reserves. Indeed, they have done very well building up these reserves in the previous years, and that was a very smart decision, but in the long run I would not envy Mr Putin. The fact that he says that he can do what he wants and Russia cannot be blackmailed or humiliated means either that he does not understand the numbers or that he pretends that things are better than they are. I think he does understand the numbers, and that is why Donetsk and Lugansk are not part of Russia.

Q86 The Chairman: Thank you very much, Mr Guriev. Can I ask a final question? Back in 2010, Mr Putin suggested the creation of a free trade area from Lisbon to Vladivostok, with enhanced co-operation in research and technology and enhanced industrial co-operation. Do you think the EU reacted sufficiently positively to that proposal? Do you think it would still be of interest to Moscow? Could it be a project for carrying forward in the long term a constructive relationship between the EU and Russia?

Professor Guriev: It is a very good idea. I do not think Russia should join the eurozone—all we know about optimal currency areas suggests that Russia should not be in the eurozone—but a free trade area is a completely different story. It is a great idea and it should be pursued. The EU has not reacted to this aggressively enough. The EU should have devoted more resources to this conversation. The EU was busy with other things in 2010. If you go back to 2010, many people were saying that the eurozone would not survive and so on, so in that sense it is understandable. Is it a vehicle for forward-looking constructive EU-Russia relations? Yes, but maybe not with this set of players in their offices. Right now, I do not see how sanctions can be removed completely. I do not see how, therefore, there will be a free trade area. In that sense, maybe with some other political leaders we will see a change but not now. In the long run, I think it should happen and it will happen.

The Chairman: Mr Guriev, we have covered a very great deal of ground and we have done it in slightly less than an hour, so I would like to thank you very much for that. I was told that you might wish to make a statement in private and, if you did, that we would ask the people behind you to leave. If you do, that would be fine, but if not I will thank you for what you have given us.

Professor Guriev: Let me say something, if I may. There was a question about Western companies doing business in Russia in the Russian way. I can just briefly say something in public about that. I would like to say in public that in general Western companies are doing business like they would do business in Europe or the US, and Western companies in Russia set examples of meritocratic and honest organisations. However, there are exceptions. Those exceptions have been prosecuted in the West in some cases, like Daimler and Siemens, but there is another exception that I would like to bring to your attention, which is not an English company but a continental European company: Yves Rocher, the cosmetics firm. This company is now helping the Russian Government to put a political opponent in jail. This company has initiated a criminal investigation against Mr Navalny, who is now under house arrest because of this case. We think that this company was threatened by Russian investigators and that, because of that threat, the company started that case. Later on, this company did an internal analysis and came up with an internal document that suggested that Mr Navalny and his brother, who has also been investigated, are not guilty of any wrongdoing, and yet this case continues and the company continues to be a party in the case, which is a clear case of political persecution in Russia. Examples like this undermine respect for Western businesses, and they should be made public and discussed.

Other than that, I would say that in general Western companies are a beacon of light in the business environment. That makes them less competitive, because Russian businesses that

follow the Russian way of doing business and give bribes get better deals, but in the long run it is the only right way to do business, whether it is in the West or in Russia. Thank you.

The Chairman: Mr Guriev, thank you very much indeed.